IN THE MATTER OF PART 3 OF THE
***LEGAL PROFESSION ACT*, RSA 2000, c. L-8**

AND

IN THE MATTER OF A HEARING REGARDING
THE CONDUCT OF BRIAN DOHERTY
A MEMBER OF THE LAW SOCIETY OF ALBERTA

Hearing Committee

Cal Johnson, QC – Chair
Linda Long, QC – Bencher
Nick Tywoniuk – Adjudicator

Appearances

Kelly Tang – Counsel for the Law Society of Alberta
Roy Nickerson, Q.C. – Counsel for Brian Doherty

Hearing Date

December 7 – 8, 2020

Hearing Location

Virtual Hearing

HEARING COMMITTEE REPORT

Overview

1. Brian Doherty (Doherty) is a member of the Law Society of Alberta (LSA), admitted in September 1982. On December 7 and 8, 2020 a Hearing Committee (Committee) convened a hearing (Hearing) into the conduct of Doherty, resulting from a LSA Conduct Committee Panel decision of October 22, 2019 directing the issuance of the following citations against Doherty:

    1. It is alleged that Doherty failed to properly supervise his legal assistant and bookkeeper, D.D, and that such conduct is deserving of sanction;

    2. It is alleged that Doherty failed to comply with Rules 119.21(2) and 119.21(3) of the LSA by signing withdrawals from his firm's trust account without first ensuring that the conditions precedent for those withdrawals existed and that such conduct is deserving of sanction;

3. It is alleged that Doherty failed to comply with Rule 119.21(5) of the LSA by failing to withdraw funds from trust within one month of said funds being payable to the firm and that such conduct is deserving of sanction;

4. It is alleged that Doherty failed to comply with Rule 119.24(1) of the LSA by failing to maintain money on deposit in his firm's trust account in an aggregate amount sufficient to meet all obligations, and that such conduct is deserving of sanction; and

5. It is alleged that Doherty failed to comply with Rule 119.36 by failing to properly maintain his firm's prescribed financial records, and that such conduct is deserving of sanction.
(collectively, Citations)

2. Since 1994, Doherty associated in practice as a partner with Mr. Ronald Schuldhaus (Schuldhaus) and carried on a practice primarily in the areas of family law and civil litigation. Their firm is currently known as Doherty Schuldhaus, LLP (Firm).

3. In October 2017, the LSA's Trust Safety Department notified Doherty, as the Firm's designated Responsible Lawyer under the LSA's Trust Safety Rules, that it proposed to conduct an audit of the Firm's financial records.

4. The audit was scheduled to start on October 23, 2017. Doherty provided the auditor with a copy of a letter he discovered that morning upon arrival at his office. The letter, dated October 20, 2017, was authored by DD, the bookkeeper for the Firm and a legal assistant to Schuldhaus. It confirmed she had misappropriated monies entrusted to the Firm over an extended period of time, but that all such trust monies had been repaid and she was resigning immediately.

5. Attached as Exhibit 5 to the Exhibit Book, and entered into evidence at the Hearing, was a Statement of Admitted Facts and Exhibits (SOAF) which contains a detailed description of the relevant facts and circumstances applicable to the Citations and this Hearing. This Report will refer selectively to certain of those facts most pertinent to this Report.

6. DD had been a longtime employee of the Firm in its various incarnations since 1988. DD was the sole employee of the Firm having responsibility for internal accounting and bookkeeping since approximately 2002.

7. DD's extensive responsibilities as bookkeeper encompassed overseeing the Firm's accounts receivable and accounts payable and related reporting. During the operative times, the Firm was utilizing accounting software knows as ESILaw for purposes of its trust accounting.

8. After DD's brother encountered financial difficulties, she sought to assist him by misappropriating trust funds, beginning in approximately 2007. She effected this by writing trust cheques from various estate files to her brother's company. She concealed the misappropriations by depositing trust funds from new estate files to cover prior misappropriations through a "lapping scheme" that carried on until approximately October 2017. Over time, she misappropriated approximately $316,000. It was subsequently determined that she had paid this entire amount back at approximately the same time as her resignation.

9. The LSA served a demand upon the Firm for more detailed information on the misappropriation. In response, the Firm retained an independent forensic accountant ([T]) to assist in answering those questions and to provide advice on how to address procedural and control issues that might have facilitated the misappropriation. On May 30, 2018, [T] provided his report directly to the LSA, without any prior review by the Firm ([T] Report). The summary conclusions of that report are set out in paragraph 44 of the SOAF. They include that: (i) DD conducted a lapping scheme as described in her interview with LSA Investigators; (ii) DD under-recorded invoices and payments in order to make trust reconciliations balance; (iii) the misappropriation was skillfully concealed, *"based on DD's knowledge of the review and control procedures completed by Doherty and Schuldhaus";* and (iv) the misappropriation would have been detected by a control procedure of comparing the ESILaw client trust ledger cards on an estate file (Cards) with the trust reconciliation statements of monies received and disbursed prepared on that file (Statements) and recommended that be done in the future.

10. The LSA conducted several investigations on its own and issued a Trust Safety Audit Report December 20, 2017 (Audit Report) that listed nine areas of risk collectively representing a "medium risk to the safety and security of the funds entrusted to the Firm". The LSA Senior Manager, Regulation issued an Investigation Order on October 24, 2017 into, inter alia, the conduct of Doherty and the following allegations arising from the misappropriation:

    a. Misappropriation or wrongful conversion of trust funds;

    b. Failure to ensure trust transactions properly recorded in law firm accounting records;

    c. Failure to properly monitor law firm trust accounts; and

    d. Failure to properly supervise staff.

    [BO], the forensic investigator appointed by the LSA, (LSA Investigator), issued an investigation report dated October 29, 2018 (IR Report). The IR Report concluded that (i) there had been a misappropriation that had not been detected by either Doherty or Schuldhaus and that the concealment method made the shortage difficult to detect; (ii)

there was evidence the trust transactions were not properly recorded, but it was unclear to the investigator whether this rose to the level of misconduct; (iii) there was evidence that the lawyers failed to properly monitor the Firm Trust Accounts, but it was unclear to the investigator whether this rose to the level of misconduct; and (iv) there was evidence that the lawyers failed to properly supervise staff, but it was unclear to the investigator that this rose to the level of misconduct.

11. On May 11, 2020 the LSA Investigator authored a memo to LSA Counsel providing comments on the [T] Report and raising some questions or concerns therewith (LSA Investigator Memo), including (i) the trust shortage could have been detected not only by a comparison of the Cards with the Statements, but as well might have been detected by a more thorough review of monthly trust listings where there were, in some cases, relatively large discrepancies; and (ii) disagreement with a conclusion by [T] that a review of cheques and trust transfers between files would not have detected the misappropriation. The LSA Investigator agreed that the misappropriation *"was at the more difficult end of the spectrum to detect"*, but lists a number of procedures/controls commonly used by lawyers that he indicates would have prevented or detected the misappropriation, including: (i) a separation of duties between the person doing the accounting and the person handling funds, and (ii) required vacations for applicable staff personnel with other staff personnel trained to fill in those roles while others were away.

12. After reviewing all of the evidence and exhibits, and hearing the testimony and arguments of the LSA and Doherty for the reasons set out below, the Committee finds Doherty not guilty of conduct deserving sanction on in respect of each of the Citations.

Preliminary Matters

13. There were no objections to the constitution of the Committee or its jurisdiction. None of the parties or other persons requested a private hearing.

Review of the Evidence

14. In addition to the direct evidence provided at the Hearing, the Committee also referred to a number of other sources for a determination of the relevant facts, including the IR Report (and the transcripts of interviews of DD, Doherty and Schuldhaus by LSA Investigators contained therein), the SOAF and the various exhibits entered into evidence at the Hearing.

15. Beginning with the SOAF, the Committee particularly notes the following:

    a. DD was the Firm's sole bookkeeper and accounting employee from about 2002 until her 2017 resignation, in which capacity her duties included (i) overseeing the Firm's accounts receivable and payable and all related reporting; and (ii) preparing monthly trust reconciliations and all related trust accounting and reporting duties.

b. In her capacity as legal assistant to Schuldhaus, DD was responsible for managing his estate practice, including preparing all financial reporting required for estate files, including all Statements (paragraph 22). She was the only individual handling estate files and no other assistant would have had the opportunity to view those files or detect discrepancies. DD only went on vacations of a week or less and no one else worked on her files while away (paragraph 32.j & k).

c. During the relevant period, the Firm utilized ESILaw for its trust accounting software (paragraph 23).

d. DD forged the lawyer's signature on certain trust cheques she used to effect the lapping and misappropriation scheme (paragraph 30.c).

e. DD could not remember the number of trust files involved in the misappropriation but ball parked that *"maybe 10, (but) 99.9% of the estate files were perfect"* (paragraph 30.g).

f. DD would lap accounts to cover trust shortages on a file prior to any distributions being made on a file and would typically lap accounts on two estates at a time (paragraph 32.d & e).

g. On the impacted estate files, the Cards showed the actual transactions that occurred on the file, including misappropriations. However, it was not Schuldhaus' practice to compare the Statements with the Cards (paragraph 32.f & g).

h. The Firm did not have a procedure in place requiring lawyers to review the Cards. The lawyers placed complete trust in the Statements prepared by DD (paragraph 55).

i. Schuldhaus reviewed the Cards for estate files on occasion, observed corrections on occasion, sometimes asked DD for explanations for mis-posting and would believe explanations provided (paragraph 59).

j. Schuldhaus did not often compare the Statements and the Cards, and as such did not detect discrepancies (paragraph 60).

16. From the IR Report, the Committee particularly notes the following:

a. DD Interview

i. The lawyers would not have realized the trust shortages because money was constantly coming in and going out, so there was a constant volume of transactions (page 30). If Schuldhaus looked in the estate files, he would see that the actual Statements were correct and he would see (at final distribution) that all the cheques were there and all the receipts were there (page 57). If Schuldhaus was more detailed, he may have caught it but likely missed it because of the volume (page 84).

ii. Schuldhaus did not compare the Statements to the Cards but if he did and asked DD she would have said, *"Oh shit, I must have put that in the wrong place, I'll fix it right now, but that never happened"* (pages 57-58).

b. Doherty Interview

i. This was the perfect storm. DD did estates, the Statements and the bookkeeping. Doherty had no reason to believe there was a problem (page 39).

ii. Doherty did not know Schuldhaus' process for reviewing and monitoring estate files. Doherty believed they both completely relied on DD (pages 74-75).

c. Schuldhaus Interview

i. They (Doherty and Schuldhaus) believed DD covered the shortage by moving monies between trust accounts. She was able to do that because estates had money sitting and nobody else looked at them. Commercial and real estate files were done by other paralegals, so if money was misappropriated there, somebody would have noticed (page 19).

ii. Schuldhaus discussed the Statements with clients. Occasionally he looked at ESILaw and saw corrections, but it did not occur to him someone there for 27 years was lapping. He saw mis-postings on real estate files, but just wrote them off to human error (pages 23-24). On occasion, he would ask, "*like*, *what happened here? Oh, it just went into the wrong account, it should have gone into this account"* was the answer he got and it is the answer he believed (page 24).

iii. Sometimes Schuldhaus compared the Cards to the Statements, but not often (page 28). Something like ESILaw, it's not that he would be unfamiliar or not able to figure it out but it's just that he never spent the time to really learn exactly how the program worked (page 25).

iv. Schuldhaus may have failed to supervise if there was a requirement to look at Statements every time something happened on a file. He relied on the Statements. Even if he looked at ESILaw, he may not have caught a problem (page 71).

v. It never occurred to Schuldhaus to go and look on a spot check on a monthly or a bi-monthly basis at the money going in and out because touching the file when an interim distribution happened, touching the file at the end when the final distribution happened, that was the modus operation for those types of files (page 70).

vi. It is clear now to Schuldhaus that having one person do the estates and then the same person doing the accounting was how this all came about. (page 73) On an estate file, the timelines were longer, DD was the one who had the ability to do the postings and nobody else would look at that. It is fair to say that she had control over everything on these files (page 74).

17. From the evidence provided by witnesses at the hearing:

a. [CU] – Manager of Trust Safety for the LSA (Trust Safety Manager)

i. Ms. [CU] acknowledged that (i) in large firms the accounting and trust duties are often delegated to support staff. That segregation of duties makes it much easier for them than for small firms to prevent or detect misappropriation, and (ii) while some delegation of duties is specifically permitted by the Rules of the LSA (Rules), that is not a permission to delegate oversight. Lawyers are entitled and expected to trust staff, but at the same time must verify that duties are carried out correctly.

ii. When the LSA Trust Safety department conducts an audit, such as was conducted in October of 2017 in respect of the Firm, this is a compliance audit to determine compliance with the Rules, but it is not designed to, and most likely will not, detect fraud or misappropriation.

iii. A breach of the Rules detected in an audit is simply an indication of heightened risk deserving attention. This particular audit disclosed medium risk – non-compliance was not pervasive. Evidence of breaches typically leads to coming up with a remedial action plan as a result of an audit report.

b. [BO] – LSA Investigator

i. While a Statement is easier to read than ESILaw, since it is a summary of the numbers, it does not show the actual transactions. In his experience, lawyers print out the Cards and place them on the file to make sure they bill all disbursements and to make sure everything is done to close a file properly.

ii. It was difficult to detect this fraud because of the large number of clients, but it could have been detected with a review of the Cards. He acknowledged that Doherty, as the Firm's designated Responsible Lawyer with Trust Safety, would not necessarily be able to detect the fraud if it is not actually happening on one of his own files, but Schuldhaus should have *"almost 100% of the time by looking at the Cards"*. To pay out money you need to know you have money to pay out and that requires a review of the applicable Cards.

c. Schuldhaus

i. Schuldhaus acknowledged he had been to a seminar concerning theft and was told that 85% of theft in relation to law firms is internal by employees;

ii. He looked at the Cards from time to time, such as when new paralegals had started. In answer to a question as to whether he looked at the Cards he indicated *"of course I did, many times".*

iii. When Estate files concluded, he would look at the Statement to decide whether to charge the standard tariff fee;

iv. On cross-examination, Schuldhaus said he often looked at the Cards but thought that where DD was manipulating files she hid those ones from him – after 25 years he was not concerned about DD. *"The very few files DD didn't want me to see, I wouldn't see"*. If he saw something, DD would just say that she would fix it and he would accept that.

v. Real estate paralegals would often make accounting mistakes on their real estate files such as depositing a cheque with the wrong bank, but DD would always fix these and provide an explanation.

vi. He would only look at the Cards if there was an interim distribution or at the time of finalizing the file and distributions. He said interim distribution did not happen often; it was rare for large amounts to flow out other than at the time of final distributions. He acknowledged that interim distribution to beneficiaries would be unusual in the middle of a file. That would have

been a red flag, but he expected DD would have just said it was a mistake which she would fix.

vii. Schuldhaus did not detect what DD was doing because no clients complained about missing monies.

viii. He would have 30-40 estate files on the go and DD was only playing around with three or four, so he would not see the problems.

ix. When asked about the seeming contradiction between paragraph 60 of the SOAF (indicating that he rarely looked at the Cards) and his direct evidence of looking at the Cards often, Schuldhaus indicated paragraph 60 referred to his answers during the interview for the IR Report and at that time he did not understand the number of files involved.

d. Doherty

i. In answer to a question concerning confidence that monies were being properly accounted for, Doherty indicated that each lawyer had to be familiar with his own files but that he also relied on his accountant at the time of year end and as well on clients to serve as a check.

ii. Doherty indicated each lawyer needed to know where the money came from on his own files and where it was going.

18. Doherty and the LSA submitted the SOAF evidencing factual matters on which they agreed. The Committee notes the following from the SOAF, or the evidence provided at the Hearing, on which there appears to be agreement:

a. The lapping scheme devised by DD was sophisticated and was difficult to detect due to the large number of clients involved, the relatively large number of transactions, but also due to DD's knowledge of the review and control procedures of Doherty and Schuldhaus;

b. The lapping scheme could have been detected by reviewing the Cards against the Statements, at least at the time of an interim or final distribution, although Schuldhaus alleges that DD would have explained the inconsistencies away;

c. The integrity of Doherty or Schuldhaus was never in issue;

d. The success of DD's scheme with relation to estate files was dependent on (i) her having sole authority with respect to the accounting and trust matters on estate files including the handling of receipts and distributions and the preparation of Statements for review by Schuldhaus; (ii) her practice of not taking

holidays more than a week long and not having anyone cover the estate files during any of those holidays; and (iii) DD forging lawyer signatures on certain trust cheques that she used to assist in the lapping scheme;

e. No clients of Schuldhaus at any time suffered any monetary loss from the lapping scheme due to DD's ultimate replacement of the funds she had misappropriated;

f. The Rules and the Code of Conduct (Code) contemplate the delegation of duties such as accounting and bookkeeping to non-lawyers, but with an attendant duty of proper supervision; and

g. While the Statements appeared to balance, they did not show the real story. A review of the Cards was necessary to show the fraud as they contained the actual story of what had happened on the lapping scheme.

19. It appears that there was some substantial disagreement, or at least confusion on the evidence, on the following factual matters:

a. The extent to which Schuldhaus reviewed the Cards on some basis. In the SOAF, DD's statements to the LSA investigator were to the effect that *"the law firm did not have a procedure in place requiring lawyers to review the ESILaw client trust ledger cards for their client files. The lawyers placed complete trust in the Statements of Monies Received and Disbursed prepared by DD" (*paragraph 55).

Also from the SOAF, at Paragraph 60, Schuldhaus indicated in his interview with the LSA Investigators that he did not often compare the Cards to the Statements and as such did not detect the fraud. As noted above in paragraph 19(f), on cross-examination, Schuldhaus indicated he looked at the Cards *"often"*, *"many times"* and *"would only look at the Cards if there was an interim distribution or at the time of finalizing the file and distributions"*.

The LSA Investigator indicated that, at least at the times money is paid out, there should have been a review of the Cards to ensure there was actual money to pay out, which only the Card could verify. His evidence was to the effect that Schuldhaus should have "100%" been looking at the Cards at that time; and

b. Both the Trust Safety Manager and the LSA Investigator indicated that the LSA audit conducted in October of 2017, or indeed as conducted in any circumstance, is not designed to, nor necessarily can, detect fraud. That requires a forensic audit.

20. The evidence of the LSA Investigator included:

a. In his experience, lawyers managing a file usually reference the Cards when it is time to close a file so that they make sure they bill all disbursements, make sure the file is properly closed and to make sure the applicable trust account is zeroed out at the time of closing;

b. This law firm was unusual in the large number of inactive trust balances over two years old which caused its trust listing to be very large; and

c. It is the responsibility of the lawyer actually handling the file to look at the Cards. The Responsible Lawyer looks at month end trust reconciliations and supporting documents.

Submissions of the LSA on Citation 1 for Doherty

21. LSA Counsel submits the following:

a. LSA Counsel referenced the SOAF, contended that there were explicit admissions of failure to supervise, and noted that in general the reviews conducted by Schuldhaus did not go beyond the Statements. The improper transactions were clearly evidenced in the Cards, but Schuldhaus did not detect that by reason of a lack of review;

b. An individual lawyer is the only person held accountable by the LSA as that is the only person it regulates, not the paralegal. The only reason DD had the access that allowed the misappropriation was because the lawyers provided it to her without proper supervision. The delegation process must be accompanied by supervision; and

c. The Trust Safety Manager and the LSA Investigator gave a number of examples of procedures or policies that, if implemented, could possibly have mitigated, or provide earlier detection of the misappropriation.

Submissions of Counsel for Doherty on Citation 1

22. Counsel for Doherty submits the following:

a. As integrity was not in issue, that raised the bar for the LSA in terms of attributing culpability. Employers are entitled to trust an employee. The evidence showed the trust wasn't misplaced and that should discharge the reverse onus; and

b. Lawyers are entitled to trust their employees. The standard here is not one of perfection. Ignorance of the fact of the shortage is not conclusive since we are not dealing with a strict liability offence.

Analysis and Decision

Preliminary Questions to Counsel

23. The Committee, after the conclusion of the Hearing put a number of questions to Counsel for both parties in relation to the burden of proof, available defences and some procedural fairness questions as follows:

    1(a). Section 67 of the *Legal Profession Act (Act)* is very generally stated and seems to apply to the Trust Accounting Rules (119) citations; is it also applicable to the failure to supervise citations?

    1(b). Specifically with respect to section 67, is it an unchanging burden or a shifting burden of proof? If the burden shifts, then what is the basis of the shift and the implication on the standard of proof?

    2. With respect to section 67, what defences are available, and under what circumstances? Can a defence of reasonable or due diligence be raised? If the defence is available and made out, what burden falls on the LSA?

    3. Is there an obligation for procedural fairness in the Trust Safety process, and if so, does that differ from that applicable generally in LSA conduct proceedings?

24. In answer to these questions, LSA Counsel responded in summary as follows:

    a. Question 1(a):

        i. Section 67 of the *Act* indicates that where a member of the LSA has received money in trust then the burden of proof of establishing that such money has been properly dealt with lies with the member. The failure to supervise citation invokes this burden since it is expressly related to the handling of trust funds;

        ii. DD was only able to perpetuate the fraud because of the broad delegation that had been made to her, but without the requisite supervision that was required under the Code (Section 3.5-1) and the Rules (119-119.46); and

        iii. The intent of section 67 is compromised if its application to trust accounting duties under the Rules can be avoided by simply delegating to an employee.

    b. Question 1(b):

i. While section 67 shifts the burden of proof, the standard of proof remains the same for the member – proof on a balance of probabilities; and

ii. Beyond that, the burden of proof on the member and standard of proof required of the member remain the same throughout.

c. Question 2:

i. Section 67 does not impose strict liability in relation to the failure to supervise and, accordingly, no defence of reasonable or due diligence is engaged. Rather the member must show on a balance of probabilities that the money entrusted was dealt with in such a manner that the conduct in doing so did not rise to the level of sanction; and

ii. To demonstrate trust monies were properly dealt with requires evidence of proper dealing in accordance with the above referenced provisions of the Code and Rules. Proper delegation required the types of controls cited by the LSA Investigator, but which Schuldhaus and Doherty did not adopt in their practice.

d. Question 3:

i. There is a limited duty of procedural fairness in Trust Safety proceedings in comparison with other LSA conduct proceedings. The *Act* expressly provides for certain procedural fairness protections in conduct proceedings that are not made applicable to trust safety matters;

ii. The Rules themselves set out the procedural fairness requirements in Trust Safety proceedings and these are generally limited to rights of appeal and to receive a written report of proceedings; and

iii. Common law procedural fairness supports the conclusion that the duty of fairness owed in Trust Safety proceedings is similarly limited.

25. In answer to the questions of the Committee, Counsel for Doherty submitted the following:

a. Questions 1(a) and 1(b):

i. Counsel suggested there are three types of statutory offences: strict liability, absolute liability and offences that require mens rea. The offences here are at most strict liability.

ii. As a strict liability offence, it is open to Doherty to show in defence that he took all reasonable care. Having done so, it falls on the LSA to establish on a balance of probabilities that the conduct was unreasonable – meaning that it was unreasonable to trust the fidelity, accuracy and competence of DD.

b. Question 3:

i. Relying on Supreme Court of Canada authority dealing with procedural fairness, and considering particularly the cited factors of the importance of the decision on the impacted individual, and the legitimate expectations of the member to procedural fairness, Counsel for Doherty suggested Doherty could expect procedural fairness in every aspect of the proceeding.

ii. If the Committee did not accept the reversal of the onus, once Doherty had shown reasonable care, then that would constitute procedural unfairness.

Burden and Onus of Proof

26. In reviewing the submissions of both Counsel on the question of the application of section 67, the Committee considered the LSA conduct decision, cited by LSA Counsel, in *Law Society of Alberta v. Skrypichayko*, 2016 ABLS 57. In that case, counsel for the LSA tried to invoke the reverse onus provisions of section 67 on the basis that facts internal to an investigation that took place revealed that there might have been a mis-handling of trust money. However, at the outset, the citations issued did not address that. As the hearing committee in that case noted: *"He was not, however, cited for failing to properly deal with either trust money or money that ought to have been characterized as such and placed in trust. The reverse onus provision in section 67 does not apply."*

27. However, this is a case where the citations deal with a failure to supervise specifically in the context of dealing with trust money. Accordingly, the reverse onus provisions of section 67 do apply and the burden of proof in this case is upon Doherty to establish, on a balance of probabilities, that he did properly supervise DD. In this determination, the Committee is in agreement with the conclusions of the hearing committee in *Law Society of Alberta v. Elliott* as cited in paragraph 30 of the Queen's Bench appeal decision found at *Law Society of Alberta v. Elliott*, [2002] L.S.D.D. No. 53. *Law Society of Alberta vs. Murray Engelking* 2009 LSA 18 (Engelking) also involved an employee misappropriation and the citations were similarly worded in terms of failing to provide meaningful and effective supervision of staff. Without examining the question or referring to any argument or discussion on the point, the hearing committee in that case simply noted that the onus was on the LSA to prove the allegations on the balance of probabilities. The Committee respectfully disagrees.

28. The Committee next addresses the contentions of Counsel for Doherty that this failure to supervise is a strict liability offense and thus subject to both a shifting of the onus to the LSA, and a reasonable diligence defense on behalf of Doherty. The Committee concurred that the citations against Doherty relating to specific provisions of the Trust Safety Rules could be characterized as strict liability offenses. However, Citation 1 does not arise from the provisions of the Trust Safety rules, but rather from the general Code obligations. Specifically, the provisions of Section 3.5-1 and Section 6.1 of the Code deal with the obligation of a member to supervise those to whom the member delegates tasks and functions and for whom the member has full personal responsibility for their delegated functions. Section 119.3(1) (d) of the Rules confirms this ultimate liability of a member for the actions of a delegee. However, no citation was issued for Doherty for breach of this provision.

29. The Committee notes that, in the case authorities dealing with section 67 and the burden of proof, (i) there were no suggestions of a strict liability offense arising from a failure to supervise, (ii) nor any defense to due diligence independent of the obligation to properly supervise. In the various case authorities cited dealing with failure to supervise citations, the Committee also noted no suggestion or finding that such a citation is a strict liability offense nor subject to a simple due diligence defence.

30. It is noteworthy that the Code provisions cited above have only been in place in those specific forms since June 2015. Prior to that, the applicable Code provisions were found in a version dating from February 2007. Section 4 of Chapter 2 dealing with Competence indicated that*: "A lawyer may assign to support personnel only those tasks that they are competent to perform and must ensure that they are properly trained and supervised. Supervision of every employee must be meaningful and effective".* Although worded in briefer fashion, the substantive obligation is similar. In any event, the lapping scheme continued for several years after the Code provisions changed and the current Code provisions governed Doherty's obligation.

31. The Committee interprets section 67 to indicate that Doherty must show on a balance of probabilities that he did properly supervise, not that he had an obligation to show in an absolute sense that the trust monies were properly dealt with.

Citation 1

32. The duty is not simply to supervise, but to supervise "properly". A review of the cases cited by Counsel was not instructive in relation to an understanding of this term. The Oxford English Dictionary defines it as "correctly or satisfactorily", in the context of a requirement that work be carried out "properly". The Cambridge English Dictionary defines it as "correctly, or in a satisfactory way". The cases cited by counsel for the LSA largely dealt with situations where the member admitted a failure to supervise by way of a statement of admitted facts or in direct testimony during the hearing. In addition, most

of the case examples provided demonstrated such an egregious delegation of responsibility or dereliction of duty that the examination of the precise requirements for meeting the standard were not considered in any comprehensive way or through any substantive analysis of the supervisory diligence mandated. The dictionary definitions seem to import something more than mere oversight. They suggest that the standard required is in some fashion linked or related to the manner in which a duty or task is carried out and the results obtained.

33. In the concurrent decision of the Committee on Schuldhaus, it was determined that Schuldhaus was guilty in respect of a failure to properly supervise citation worded substantially the same as Citation 1 in this Hearing. Having come to that conclusion however, the Committee must independently make a determination of the guilt or innocence of Doherty in relation to Citation 1.

34. The expert evidence provided, both on behalf of Doherty and the LSA, noted that the misappropriation was skillful in that certain standard control procedures such as comparing the Statements to various supporting documents would not necessarily have disclosed any concerns. Similarly, month end reconciliations of the bank accounts and trust balances on the trust listings would not have disclosed any issues. Taken together they would have balanced. The Statements were shared with clients to ensure that they were in accord with the distributions. Over the whole time of the misappropriation, no completed and closed files were short funds, nor were any client complaints received. The LSA Investigator Memo and the evidence of the Trust Safety Manager suggested a number of different ways that the misappropriation could possibly have been **prevented** using various procedures involving segregation of duties and various monitoring processes. However, the issue in terms of the wording of Citation 1 is more appropriately, what would have **detected** the misappropriation? Again, the LSA Investigator and the Trust Safety Manager provide some methodologies that might possibly have detected the misappropriation, but the Committee found all but one of these suggestions were not overly helpful in the analysis. [T] and the LSA Investigator (Accounting Specialists) held differing views on whether several alternate reviews could have detected the misappropriation.

35. However, the Accounting Specialists do agree, and it seems uncontroverted, that the Cards, in each of the files involving misappropriation, did demonstrate the divergence between what the Statements purported to show happened and what in fact did happen. Would a reasonable review of the Cards have disclosed the misappropriations? As stated in the [T] Report: *"The control which would have detected, at the very least, irregularities in the accounts and likely would have detected the misappropriation would have been to compare the Ezi-Law client record to the Reconciliation of the client's account provided to the client on a periodic basis or at the conclusion of the file."* As noted in the LSA Investigator Memo, *"I completely agree with this. Had the lawyers compared the two documents, they almost certainly would have identified irregularities, and if followed up on, would likely have detected the misappropriation"*. Such evidence in

this case assists in indicating a standard of supervision that would have had the appropriate result. This is in contrast to the situation in *Engelking*, which dismissed the applicable citation as no evidence was led as to an accepted standard of supervision and training (*Engelking*, paragraph 60).

36. The Committee notes the following factors pertinent to the question of assessing the duty of proper supervision in this case:

    a. Schuldhaus indicated that he understood and frequently referenced the Cards;

    b. Schuldhaus' practice was to do a comparison between the Cards and the Statements often and, in any event, at least as often as the interim and final distributions on an Estate file;

    c. The Cards were not complicated in the sense that, even over the course of an extended Estate file, Schuldhaus acknowledged that they were still not more than a page or two;

    d. The Accounting Specialists testified that a comparison would have detected the misappropriation and that this type of comparison was a recommended and appropriate exercise;

    e. The Firm allowed a substantial delegation of authority to DD without a segregation of duties that would have made this misappropriation much more difficult and which segregation of duties was in evidence elsewhere in the Firm in relation to the handling of trust funds in its real estate practice;

    f. Schuldhaus had attended at least one accounting client presentation prior to the misappropriation that indicated that 85% of theft was occasioned by internal personnel;

    g. Schuldhaus would have accepted whatever explanation DD would have provided in relation to discrepancies identified as a result of a comparison of the Statements to the Cards or as a result of a basic examination of the Cards from time to time;

    h. Both the LSA Investigator and Doherty in their evidence indicated that the type of detailed supervision that would have been required in this case would have been the responsibility of the lawyer who was conducting the file and would not reasonably have been expected of the lawyer designated with the LSA as its "Responsible Lawyer";

    i. ESILaw was a LSA approved legal software vendor; and

j. Tabs 13-14 and 33-35 of the IR Report illustrated six different illustrative comparisons of Statements to the applicable Cards, going back over the period covered by the [T] Report. In some cases, such as the [P] Estate and the [B] Estate, the discrepancies were relatively smaller amounts and more difficult to detect. In four other cases, the discrepancies were more evident, and involved substantial sums of money where a comparison would more readily disclose the discrepancies.

37. It is the conclusion of the Committee that the primary duty to supervise DD rested with Schuldhaus, given (i) it was on his files that the misappropriation occurred, and (ii) the various opportunities which were essentially open only to him to conduct the examination of the Cards that would have detected the misappropriation. It appeared clear that Doherty conducted a number of usual and expected reconciliations and reviews in his capacity as the Firm's Responsible Lawyer, but which did not include the Cards comparison.

38. It is clear that the duty of proper supervision is imposed on individual lawyers. However, as a matter of practicality in the context of this firm, it would be impractical and unreasonable to suggest that both Schuldhaus and Doherty were obligated to carry out a co-extensive level of supervision of DD. Quite reasonably, they had segregated their roles and the more specific duty of supervision rested with Schuldhaus. In the circumstances, the Committee concludes that Doherty had a lesser obligation of supervision that he adequately discharged in relation to DD.

39. Doherty has satisfied the burden of proof of demonstrating, on a balance of probabilities, that his supervision amounted to proper supervision of DD in the circumstances and that he is not guilty of conduct deserving of sanction in relation to Citation 1.

Citation 2

40. The SOAF, the IR Report, the [T] Report and the testimony at the Hearing focused on the issue of the misappropriation and the Citations dealing with proper supervision. Outside of the Audit Report, relatively little of the evidence dealt with Citations other than Citation 1. Briefly put, Rule 119.21(2) is a deemed certification by a lawyer authorizing a withdrawal or transfer from a trust account that everything in relation to that withdrawal or transfer has been properly done including that there is sufficient money in the trust account to cover the withdrawal. Rule 119.21(3) specifies the conditions for withdrawal from a trust account before payment either to the client, the law firm, or a third party.

41. Interestingly, Appendix A to the Audit Report makes specific reference to the Rules associated with each finding or recommendation category, but without any reference to either of these Rules. Section G of the SOAF, beginning at paragraph 61, deals with the Audit Report and references nine areas of risk and in all but one case details the applicable Rule. Again, with no mention of either of the Rules referenced in Citation 2.

42. The Trust Safety Manager in testimony suggested the requirements of Rule 119.21(2) and (3) mean that Doherty, as the Firm's Responsible Lawyer, must ensure that at all times the money that the Firm has on deposit matches the money on its books. The SOAF confirms Doherty's responsibility for signing off on the monthly trust reconciliations and reviewing the bank statements and client trust ledgers, as provided by DD, on a monthly basis to ensure that the totals balanced.

43. In argument, Counsel for the LSA referenced these Rules indicating that at various times Doherty signed cheques and that it was his responsibility to ensure that all prerequisites to such signatures were satisfied, whether on his own files or others. Generally, Citations 2, 3 and 4 deal with Trust shortages, withdrawals and transfers. The Rules engaged by Citations 3 and 4 are dealt with and referenced in the Audit Report and the SOAF, unlike Citation 2. The Committee determined that the evidence adduced at the Hearing did not substantiate Citation 2 and dismissed this Citation.

Citation 3

44. Paragraph 61(i) of the SOAF refers to the Audit Report and its finding, in relation to Rule 119.21(5), several instances where services had been rendered but funds had not been moved from the applicable trust account to the Firm's general account within a month of the Firm becoming entitled to those funds, presumably, as a result of billing the file. However, the SOAF notes the agreement of the parties that this related only to commissioning and notarization fees that were inadvertently lost sight of. Counsel for the LSA referenced this concession briefly in her argument on this particular Citation. Counsel for Doherty acknowledged the breach of this Rule in argument.

45. The Committee finds that the breach of the Rule in question has been established.

Citation 4

46. Citation 4 references a failure to comply with Rule 119.24(1) for failing to maintain trust deposits in an aggregate amount sufficient to meet all obligations in relation to such trust monies. Paragraph 61(a) of the SOAF refers to non-compliance with Rule 119.24(3) for trust shortages caused by various minor errors such as bank charges, payments made from the wrong trust bank account or trust ledger card or posting errors. The SOAF notes all of these were corrected, but not reported.

47. Rule 119.24(3) is concerned with the duty of a Responsible Lawyer who becomes aware of a deficiency to report that deficiency if either the deficiency is not corrected within 7 days of the shortage or in any event if the deficiency is greater than $2,500. The first item of the Audit Report is expressed to deal with the general issue of Trust Shortages. It refers only to 119.24(3) as the applicable Rule but also refers to the aggregate requirement referenced in Citation 4. However, it is not clear from the Audit Report

whether this is simply referring to the 25 instances of the nature referred to above, or whether it constituted other breaches of a possibly more material nature. It does indicate, "Although all shortages were corrected, they were still reportable to the LSA".

48. In argument with respect to Citation 4, Counsel for the LSA stated that there was an onus on Doherty to show that there was always money on deposit in the trust account in the aggregate sufficient to meet related obligations. Counsel for Doherty argued that a trust shortage should not be a strict liability offense and that Doherty's ignorance of these relatively minor shortages should amount to exculpation in the circumstances.

49. As with Citation 2, we face a situation where a particular Rule is specified in the Citation, while much of the evidence purports to reference a different Rule, and there is no direct concession in the SOAF as was the case with Citation 3. However, for Citation 4, there is at least reference in the Audit Report to the aggregate requirement and the undisputed fact of the trust shortage.

50. As noted earlier in this Report, the Committee considers this Citation to be in the nature of a strict liability offense. In written argument in response to the Preliminary Questions posed by the Committee after the Hearing, Counsel for Doherty argued that a defense of reasonable care may be raised in response to a strict liability offense. Without going into detail on that issue, it is sufficient to note that the Committee did not find evidence before it that would substantiate any such defense. While the Committee was concerned that Doherty was asked to respond to a Citation that appeared to inaccurately reference the Rules, we find that at least the evidence of breach was uncontroverted and had been established.

Citation 5

51. Citation 5 concerns Rule 119.36 and the alleged failure of Doherty to properly maintain the Firm's prescribed financial records. Paragraph 61(g) of the SOAF cites Rule 119.36(3)(b)(iii) for an apparently very minor breach where one general account and one pooled Trust account did not state "General" or "Trust" respectively. Paragraph 61(h) specifies Rule 119.36(5)(b) indicating that certain journals were not maintained in a consistent manner on a monthly basis. Section 7 of Appendix A deals with "Bank Reconciliations", references Rule 119.36(3)(b)(iii) and notes that the bank statements failed to make the distinction between Trust or General noted above and had been opened using a prior name of the Firm that had not been corrected. Section 8 of Appendix A of the Audit Report deals with "Records Maintenance and Retention", references Rule 119.36(5) (b) and makes the general comment that the Firm's approach to general and trust financial records lacked structure and proper organization. It then detailed some journals particularly affected by inconsistencies.

52. In argument, Counsel for the LSA did not spend much time addressing these deficiencies but referenced the long-term instances of DD doctoring the records in

pursuit of the misappropriation. Counsel for Doherty similarly did not materially address this particular Citation in argument.

53. The record before the Committee established the basis for this Citation and the Committee determined that Doherty had not discharged the onus and burden of proof applicable to him in relation to this Citation.

Sanctionable Conduct

54. Having concluded that the Trust Safety Rules referenced in Citations 3-5 were breached, the next question to address is whether such conduct is deserving of sanction. The *Act* sets out the general definition of conduct deserving of sanction (at section 49(1)):

> *"For the purposes of this act, any conduct of a member, arising from incompetence or otherwise, that (a) is incompatible with the best interests of the public or of the members of the Society, or (b) tends to harm the standing of the legal profession generally, is conduct deserving of sanction, whether or not that conduct relates to the member's practice as a barrister and solicitor and whether or not that conduct occurs in Alberta."*

55. The Hearing Guide does not address specific factors to take into account in relation to the determination of sanctionable conduct. Two considerations arise out of section 49(1) of the *Act*. Was this conduct incompatible with the best interests of the public or the members? Does it tend to harm the standing of the legal profession generally? The *Act*, the Rules and the Code demand a high level of protection when the public entrusts monies to lawyers.

56. Substantially all of the evidence in respect of Citations 3-5 arises from the Audit Report. That report concluded that all of the nine areas cited in the Audit Report constituted a medium risk to the safety and security of the funds entrusted to the Firm. The cover letter of December 20, 2017 to Doherty from the LSA stated in part:

> "These findings are itemized in the appendix to this letter along with detailed recommendation. We would appreciate your prompt attention to these identified issues as soon as possible. There is no requirement to report to the Law Society on your progress addressing the recommendations; however we encourage you to retain relevant documentation on your corrective action plans in a manner sufficient for follow up submission and/or inspection by Trust Safety".

The significance legend at the end of the Appendix to the Audit Report notes that "medium risk" evidences "moderate noncompliance" with the LSA Rules but does require some immediate attention to reduce risk exposure. The tone and tenor of these communications are such as to suggest that the issues relate to areas of regulatory compliance that are not pervasive and are easily remediable. As the Trust Safety

Manager noted in her evidence, these types of compliance audits typically lead to a plan for remediation. A breach of the Rules detected in an audit is simply an indication of heightened risk deserving of attention. However, she did not indicate that they typically, or even occasionally, result in Citations for a medium risk categorization.

57. The Exhibit Book entered into evidence contained similar past letters resulting from compliance audits conducted in respect of the law firms Doherty was practicing with, including specifically in 1999 and again in 2007. As in the Audit Report, deficiencies were noted and it appeared that Doherty satisfactorily addressed them as there was no evidence of ongoing issues followed up on by the LSA, and the LSA closed its file in October 2018. Doherty was questioned at the Hearing in relation to these past audits and the deficiencies noted. He was at times dismissive or cynical about the perceived minor or silly nature of some or the recommendations. However, he nevertheless described himself as a "rule follower" and indicated that he had complied with and tried to address all matters raised in the various audits.

58. Both the [T] Report and the Audit Report were largely preoccupied with the misappropriation and did not deal in any significant detail with the Trust Safety Rule breaches. In the summary conclusions to the Investigation Report, the LSA Investigator briefly noted the failures to properly record some trust transaction and monitor law firm trust accounts but indicated that it was unclear whether the conduct rises to the level of misconduct.

59. The Committee notes that the Trust Safety Department determined to conduct a compliance audit before the misappropriation was known. It was the issuance of the letter notifying the Firm that prompted DD to admit to the misappropriation. In the ordinary course, and absent the misappropriation, the Committee doubts that the deficiencies noted in Citations 3-5 would have resulted in the issuance of Citations. While the Committee was of the view that Schuldhaus met the tests set out in Section 49 of the *Act* for sanctionable conduct in relation to the misappropriation and the failure of proper supervision, we cannot say the same for these particular citations for Doherty. The LSA regularly conducts compliance audits and there was no evidence to suggest that a medium risk assessment results in anything more than a remedial plan of action and subsequent conduct addressing the issues identified. We cannot find the Rule breaches set out in Citations 3-5 meet either of the requisite thresholds from Section 49.

60. The Committee determines that Doherty is not guilty of conduct deserving of sanction in respect of any of Citations 3-5, and as noted above we dismiss Citation 2 in its entirety.

Concluding Matters

61. The exhibits, other hearing materials, and this report will be available for public inspection, including the provision of copies of exhibits for a reasonable copy fee, except that identifying information in relation to persons other than Doherty or Schuldhaus will

be redacted and further redactions will be made to preserve client confidentiality and solicitor-client privilege (Rule 98(3)).

Dated at Calgary, Alberta, June 4, 2021.

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Cal Johnson, QC

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Linda Long, QC

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Nick Tywoniuk