

Fraud: A growing problem affecting all lawyers

The claims reported in 2008 to date are troubling. They are troubling because of the size of the claims, and the fact that so many of them are as a result of fraud. They are also troubling because not all of the losses suffered by the lawyers involved are covered under the LAWPRO policy.

In the first five months of 2008, more than 50 claims with a fraud component have been reported to LAWPRO, compared to 35 for the same January to May period in 2007. We estimate the cost to the program of these frauds at more than \$4 million.

In addition to this, there is no easy “quick fix” way to avoid these frauds. The reality is that, as never before, lawyers have to take control of the processes and procedures in their offices and be constantly vigilant.

Many of you will already have read about, and some of you may be the victim of, two new types of fraudulent scams.

Business loan fraud

In the first scenario, a new client introduced to you by a broker or a former client, is in the process of setting up a business and is borrowing money to buy inventory or materials. The loan documentation looks legitimate and the deal is processed. A certified cheque is deposited in the lawyer’s trust account. The lawyer draws a certified cheque on his/her trust account as directed. Several days after that cheque is cashed, the lawyer is advised that the deposit cheque is counterfeit and there is a shortfall in the trust account.

Using this type of scheme, fraudsters successfully duped 10 lawyers over the Christmas and New Year holiday time. They struck again just before the May long weekend and four more claims were reported and four more lawyers were left with shortfalls in their trust accounts.

The lesson? Be extra vigilant during periods of time when there are banking holidays. When banks are closed for a day and offices are short staffed, the fraudsters have a bit more time to complete their plans.

Debt collection fraud

Equally disturbing is that these fraudulent schemes are not unique to Ontario. In Nova Scotia, an alert to members of the bar described a situation in which the lawyer narrowly missed becoming a dupe in a fraud situation. This involved a UK company asking for representation in the collection of an \$110,000 debt owed by an Ontario company. The creditor offered to pay fees of 20% of the amount collected to the lawyer.

Notwithstanding that the law firm never formally agreed to represent the UK creditor, the lawyer received a telephone call from a woman who identified herself as being the accounts payable department of the debtor company. A \$110,000 certified cheque from the company was delivered to the law firm. The cheque looked authentic, and appeared to have all the normal security features. Via email, the lawyer was directed by the creditor to send the funds, minus legal fees, to an accountant in Singapore.

This lawyer too was aware of earlier fraudulent schemes that had been reported, and before complying with the direction, he directed his staff to do some independent checking on the debtor and creditor companies.

A Google search of the debtor company revealed an Ontario company with the same name, or close to the same name; but when contacted the legitimate company advised that it did not have an office in Ottawa. A reverse phone search of the company phone number shown on the cheque showed an address for what appeared to be an apartment complex in Ottawa, Ontario. Nothing could be found about the UK company. The law firm also reviewed the bank’s website to determine if the bank address listed as a branch on the debtor cheque was shown on the bank’s website. The bank’s website did not list the address on the debtor cheque.

The lawyer then asked the local branch manager to check with the bank whose transit number was shown on the cheque, and that bank advised that they did not have a branch at the address noted. They confirmed that this was the sixth call they had received that day relating to this type of fraudulent scheme.

Lawyers are listening

The good news is that many lawyers are reading articles like this one, and paying attention to alerts, notices and emails from trusted legal sources. Many lawyers are alert to the fact that someone might be trying to dupe them, and they are developing a heightened sixth sense. Michel Castillo of the firm Advocates LLP contacted LAWPRO and wrote us the following note:

“I recall reading the Fraud Scam Alert in the Winter 2008 edition of the LAWPRO magazine. In particular I recall reading about the fake UK business man. Sure enough, a few days ago I received an unsolicited e-mail from a UK business man calling himself Bill Stevens. With the article fresh in my mind,

I followed up with Stevens. Meanwhile, I researched the company he purported to work for. It is a legitimate company, but does not do the type of work that the Stevens described. I wrote to the company to confirm whether Stevens worked there. As it turns out, surprise-surprise, Stevens does not work for that company. And strangely enough, I never heard from Stevens again."

What protected this lawyer was not simply that he was alert to the issue, but that he took several steps to assure that he was dealing with a legitimate person. In addition, he wrote back to the potential client before accepting the retainer, and requested certain information.

"Thank you for your e-mail below. We do not undertake this type of work on a contingency basis. If you would like to retain our services, we will require a CAN \$10,000 retainer. In addition to the retainer we will need:

1) the names of all parties involved in the transaction/dispute so we can undertake a conflict check;

- 2) all documents relating to the sale, including correspondence, bills of lading, receipts, invoices, proof of payment, etc.;
- 3) a telephone discussion to obtain full particulars of the potential claim;
- 4) a director's resolution from (the firm) confirming (the firm) agrees to retain our services and will undertake to pay our account.

Lastly, please advise how you obtained my name and reference. Thank you."

LAWPRO has been publishing fraud alerts since 2004, but methods of committing fraud continue to evolve. There is no simple answer to protecting your clients, your firm and yourself.

But as these lawyers have demonstrated, by being alert it is possible to avoid being the victim of a fraud. Continue to educate yourself and your staff. The more people in your firm who are alive to the unusual elements in a transaction, and who are willing to ask the next question, the better positioned you and your firm are to avoid being a victim of fraud.

Not all claims are covered

The LAWPRO policy is an errors and omissions policy and protects lawyers in the event that they have made an error in the course of providing professional services for clients. It provides coverage for claims for damages, provided that the liability of the lawyer is the result of an error, omission or negligent act in the performance of or the failure to perform professional services.

Not all claims made against lawyers are covered under the policy. If, for example, a client fell on a mat in your office and broke an ankle and subsequently sued you for damages, the LAWPRO policy would not respond. Part III (e) of the policy specifically excludes claims for this type of injury. Similarly, claims for fees and claims arising out of business ventures are among other exclusions listed in Part III of the policy.

Coverage for claims involving counterfeit bank drafts and certified cheques are not specifically insured or excluded from coverage under the Law Society insurance program policy with LAWPRO.

Under a professional liability insurance policy, LAWPRO looks to the circumstances of the claim reported to determine whether the necessary elements are there for coverage to apply, and then ensures that there is nothing within the policy that may serve to restrict or exclude coverage.

For example, this means ensuring that, under the principle insuring agreement under the program policy (Part I "Coverage

A. DAMAGES"), the claim;

- arises out of the performance of Professional Services for others,
- that the insured's liability is the result of an error, omission or negligent act,
- that Damages arise out of the Claim.

Presuming the special provisions (dealing with territory and policy period) and general conditions of the policy are met, and no exclusions apply, coverage then would be provided.

In situations in which a lawyer has suffered a shortfall in a trust account because of reliance on a counterfeit instrument, claims are likely to arise once the true nature of the instrument has become known and the instrument is declined.

To the extent that a shortfall is experienced by the lawyer's clients to whom professional services had been or were intended to be provided, coverage is generally available. To the extent that a shortfall rests between the lawyer and his/her bank, no coverage is generally available in the absence of any Professional Service having been provided to the bank.

It is very important therefore that you are alive to any potential fraud. If you have not educated your staff, please ensure that they are familiar with the indicia of fraud and that they come to you with any concerns, no matter how minor. Your trust account is the key to a successful practice.