MISPLACED TRUST

There are some important steps to take when handling trust money.

The LPLC sees numerous claims against practitioners who are alleged to have distributed trust money to a party not entitled to receive it. For risk management purposes, two critical points in time are when a client instructs a practitioner to receive money on trust and when a client instructs a practitioner to transfer trust money.

Practitioners instructed to hold money on trust need to ask the following questions:

- Who am I holding the money for?
- Why am I holding the money?
- How is the money to be held? Is it in a controlled money account or the general trust account?
- What are the triggers for payment?
- Do I need an authority or direction from someone other than the client to pay the money?

The answers should be agreed with all relevant parties and documented clearly and unambiguously.

Set the trust up properly

In one example, a practitioner acted for a vendor of vacant land subject to several mortgages and caveats on title. The mortgages were in default with a high amount of interest accruing every day.

There were various disputes between the vendor and the caveators but the practitioner acted only on the conveyance of the land. The caveators agreed to produce withdrawals of caveats on the practitioner's undertaking that the net proceeds of sale would be paid into court to await the determination of the disputes.

A week before settlement, the vendor instructed the practitioner to pay the GST amount to the Australian Taxation Office (ATO) on settlement. The practitioner then sent cheque directions showing that GST on the price was to be collected by bank cheque made payable to the ATO.

The caveators' lawyers said nothing about this direction until an hour before settlement, when they asked the practitioner to postpone settlement and have the GST cheque redrawn as payable to the court as part of the net proceeds of sale.

The vendor insisted that settlement go ahead as the purchaser threatened rescission and interest continued to accrue on the mortgages. The practitioner attended settlement and collected the GST cheque payable to the ATO. He then had a dilemma regarding whether to provide the cheque to the vendor or to the court.

This situation could have been avoided if the practitioner had been precise in establishing the terms of the trust, particularly whether "net proceeds of sale" was inclusive of GST. He needed to do this before giving the undertaking and agreeing to act as stakeholder.

Revisit the terms when instructed to pay

Even where the terms of the trust are clearly documented, practitioners need to be aware of changes to a client's ostensible entitlement to the money during the course of a matter.

In one claim, a practitioner acted for a client on the sale of her property and received the balance of the proceeds of sale into his trust account.

After settlement the distressed client informed the practitioner she had been made bankrupt on the petition of her bank. She maintained she had repaid the bank after settlement and her only creditors were a school and some minor accounts.

The practitioner said he phoned the bank and was told it would apply to set the sequestration order aside. He advised the client he would hold the money in trust pending formal confirmation her bankruptcy had been set aside.

The client later told the practitioner the bank said it had made a mistake which would be fixed. She asked the practitioner to transfer some of the trust money to her because she was being hounded by the bankruptcy trustee.

After the practitioner unsuccessfully attempted to contact the bank to confirm it was taking steps to set the sequestration order aside, he transferred the money requested by the client.

The trustee subsequently wrote to the practitioner requiring that all funds in the practitioner's trust account be paid directly to the trustee. It then became clear that the client's financial affairs were much worse than a single default to the bank.

Under the *Bankruptcy Act 1966* (Cth) the practitioner was not entitled to retain money that became the property of the trustee in bankruptcy. He should have sought the trustee's consent before disbursing the money to the client. ■

This column is provided by the **Legal Practitioners' Liability Committee**. For further information ph 9672 3800 or visit www.lplc.com.au.

TIPS

- Ensure your records accurately reflect the terms of the trust.
- Be clear about who you are holding the money for and why.
- Give your client a "dummy's" overview of your obligations.
- Be clear about the triggers for transferring the money.
- Consider whether any parties need to consent to transfer.
- Obtain consents and authorities for payment in writing.

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