

# Will Large Value Transfer Systems solve problem? Firms still prey to frauds involving fake cheques

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For Law Times

While fraudsters are increasingly moving on to more sophisticated scams, two recent decisions show the old-fashioned fake cheque is still catching out some Ontario lawyers.

In *Rogers v. Priyance Hospitality Inc.*, Ontario Superior Court Justice Ruth Mesbur ruled an unnamed Ontario law firm and its insurer must bear the loss of a \$600,000 cheque paid to an innocent third party out of its trust fund on the strength of several fraudulent bank drafts received on behalf of a client.

Meanwhile, in *Law Society of Upper Canada v. Deonarain*, a disciplinary panel of the LSUC banned a lawyer from handling client funds after his trust account was left more than \$1 million in the red following a scam that involved four counterfeit cheques.

Dan Pinnington, director of practicePRO, LawPRO's risk management arm, says an education drive by the professional indemnity insurer over the last few years has helped the legal profession keep its guard up and, in turn, driven fraudulent cheques down his priority list.

"Lawyers seem to be much more aware of this type of fraud. They're more likely to spot it, so it's fair to say it's much less of a problem than it used to be," Pinnington says.

He says Ontario lawyers are currently reporting between three and five successful scams a year to LawPRO, down from a peak of more than 20 annually earlier this decade.

Cyberscams, such as phishing or spear-phishing, where fraudsters attempt to extract sensitive information or payments by masquerading as legitimate clients or other genuine contacts of law firms, "are now a bigger concern," Pinnington says.

"But some are still falling for bad-cheque scams," he says, adding that fraudsters are constantly



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refining their approach to avoid detection.

For example, Pinnington says, in the early days of cheque scams, the scenario typically involved a suspiciously easy collection on a claim for spousal support.

By 2016, this method accounted for just five per cent of all attempts reported to LawPRO.

"There are many new ones. A lot are equipment-purchase scenarios. Debt collection and business loans are also popular," Pinnington says.

"There's no end to their imagination in terms of coming up with believable scenarios. A lot of lawyers tell us they would never fall for it, but I can tell you we've had lawyers at some of the biggest firms in the country fall for this. That's how convincing they are."

The value of continued vigilance is demonstrated by the sums at stake when fraudsters hit the jackpot by reeling in a lawyer with fake cheques.

In March, the U.S. Department of Justice announced the conviction of Toronto man Henry Okpalefe on counts of conspiracy to commit mail fraud, wire fraud and money laundering.

According to prosecutors, Okpalefe and his co-conspirators extracted \$23 million from law firms in just two years between 2008 and 2010.



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The scheme saw counterfeit cheques arriving at law firms all over the U.S., who then received instructions to wire funds on to bank accounts in Asia.

By the time the cheques were returned as fraudulent, the money had been removed from the Asian accounts and distributed to the conspirators in Nigeria and Canada, the justice department release says.

The prosecutors thanked the Toronto Police Service for their help with the investigation and warned that the scheme may still be ongoing.

The four fake cheques received by the lawyer in the *Deonarain* case had a total value of \$1.9 million, according to the LSUC decision, which says that the lawyer immediately issued certified cheques on behalf of the same client for all but \$300 of the total.

While a bank managed to recover some of the funds, that still left the lawyer's trust account short by \$1.3 million.

Granting the lawyer's request for an adjournment of an interlocutory suspension request by the law society, the panel nevertheless ruled he should not be allowed to handle client funds after expressing concern about his attitude to the scam, especially considering he had previ-

ously been duped by mortgage fraudsters.

"In his statements to the Law Society investigator and before the panel, the Lawyer blamed the bank for the fraud.

"He does not appear to appreciate his responsibility to safeguard his clients' funds held in trust and to take precautions against certified cheque fraud," chairwoman Margot Blight wrote for the panel in the Jan. 12 decision.

In *Rogers v. Priyance*, the more convoluted set of facts involved a law firm acting for Priyance, the owner of a hotel and banquet facility, in its receivership proceedings.

The law firm received a number of cheques for the benefit of its client, but it then issued payments from its own trust account before ensuring the funds had cleared, according to Mesbur's decision.

The firm had coverage for exactly that type of loss, so its insurer, AIG Insurance, launched an attempt to recover some of the funds.

Mesbur's decision concerned a \$600,000 cheque paid by the law firm to Owen Rogers, a trustee for investors owed millions of dollars by Priyance.

"This is really a case of two innocent parties suffering a potential loss as a result of the fraud of a third party. The issue is who should bear the loss. As I see it, the law firm, and thus its insurer, AIG, should," Mesbur wrote in her Dec. 14 decision.

While Rogers was in no position to know anything about the fraud, the law firm could have prevented the loss, Mesbur wrote, calling it "particularly careless" in its handling of the transaction.

Mesbur's decision highlights a number of failings in the law firm's approach, including making its disbursement at the direction of someone other than its client, and the failure to verify that person's identity or to inquire why he wanted the funds paid to third parties.

In addition, she said a close

inspection of the cheques received by the firm would have revealed numbering inconsistent with the dates they were issued and the absence of an address for the bank branch where they were supposed to be drawn.

Finally, the firm took no steps to ensure the cheques cleared before disbursing funds from its own account.

"The law firm could have avoided the problem altogether had it exercised even a modicum of care and attention," Mesbur concluded.

AIG's lawyer Reid Lester, a partner with Laishley Reed LLP, said in a statement that the insurer disagrees with the decision and has appealed.

A hearing is set for July at the Court of Appeal for Ontario in the matter.

Chris McKibbin, a partner at Toronto firm Blaney McMurtry LLP, says the threat of fake cheques was the driving force behind his firm's decision to revamp its inbound and outbound funds policy.

The firm now insists on using the Large Value Transfer System for incoming funds, a mechanism used by all large banks and credit unions that allows for instantaneous and irrevocable deposits between accounts.

"This was a risk we identified and addressed," McKibbin says.

"I think every firm should be using LVTS to the extent possible.

"You might get charged a \$200 fee, but when you're dealing with payments in the millions, it's a pretty cheap insurance policy against decisions like [Rogers]."

Although the insurer paid out to the law firm in that case, McKibbin says there's no guarantee claims will always be successful.

"Any firm, depending on whether it has some sort of crime insurance, is in a sense playing Russian roulette with this particular risk," he says.

"Our approach was to decide that it's better to try and minimize the risk of a loss in the first place." **LT**