QCAT

Queensland Civil and Administrative Tribunal

CITATION:	*Featherstone v Queensland Law Society* [2016] QCAT 205
PARTIES:	Darrell Featherstone (Applicant/Appellant) v Queensland Law Society (Respondent)
APPLICATION NUMBER:	OCR074-15
MATTER TYPE:	Occupational regulation matters
HEARING DATE:	11 January 2016
HEARD AT:	Brisbane
DECISION OF:	**Justice Carmody**
DELIVERED ON:	18 May 2016
DELIVERED AT:	Brisbane
ORDERS MADE:	**1. The reviewable decision is confirmed without variation.**
CATCHWORDS:	APPLICATIONS FOR REVIEW – review of decision to reject compensation claim – where the applicant claims compensation in respect of funds due to a third party default – where the money was deposited into a trust account – where the applicant claims to have met and reached agreements with certain third parties – where those certain third parties deny such meetings and agreements – where the applicant relies on a witness with credibility issues – whether the applicant had a right to transfer funds vested by statute in ASIC to his family trust – whether the deposit was made for investment in reliance of a misrepresentation – whether the "mortgage financing" exception is made out – whether the applicant is entitled to compensation *Corporations Act* 2001 (Cth) s 601AH *Australian Solicitors Conduct Rules* 2012 r 41 *Legal Profession Act 2007* (Qld) ss 356, 373, 392

Queensland Civil and Administration Tribunal Act 2009 (Qld) ss 2, 3, 4, 9(2)(b), 17(1), 18(1), 20, 28(1), 29, 161, 162

De Simone v Victorian Legal Services Board (Ruling No. 3) [2015] VSC 451
Edwards v Clinical Beauty Pty Ltd v Chan [2002] QDC 28
IPG Finance Australia Pty Ltd v Crouch & Lyndon (A Firm) [2012] QSC 312
Kation Pty Ltd v Lamiru Pty Ltd (No 2) [2009] NSWCA 428
Mood Music Publishing Co Ltd v De Wolfe Ltd [1977] 1 All ER 767
Sheldon v Sun Alliance Australia Ltd (1989) 53 SASR 97

APPEARANCES and REPRESENTATION (if any):

APPLICANT:	Self-represented
RESPONDENT:	M. Hinton, counsel for the respondent

REASONS FOR DECISION

[1] This is a defended application to review the decision of a statutory committee of the Queensland Law Society rejecting a compensation claim against the fidelity guarantee fund for loss of $200,000 deposited into the trust account of a law practice.

The context

[2] The applicant claims $200,000 on behalf of his family trust for monetary loss due to the default of the principal (Leach) of Gateway Lawyers (the law practice) in connection with two short term loans of $150,000 in 2009 for the alleged purpose of financing a soft drink factory (the Rong loan) and $50,000 in 2010 to finance home renovations (the Kopp loan).

[3] The larger amount was deposited by the applicant on 6 November 2009 from Jam Hair Salon's bank account and the rest was received by the law firm over three days between 31 May and 2 June 2010 in eight (8) instalments.

[4] Leach admittedly misapplied both sums.

[5] The Society decided the claim by wholly disallowing it based on the findings and recommendations of an investigative report of the fund manager that all of the money deposited into the law practice's trust account by the applicant's family trust was for the purpose of investment in reliance of Leach's misrepresentation and, therefore, was not compensable.

[6] If this is true allowing the claim would unjustifiably deplete the reserve for payment of genuine ones.

[7] The applicant asserts that the missing deposits were loan monies held by the law practice "in the ordinary course of legal practice" and cites *IPG Finance Australia Pty Ltd v Crouch & Lyndon (A Firm)*[1] in support of the proposition that a fraudulent or sham transaction does not mean that the conduct is outside the scope of that term.

The fidelity guarantee fund

[8] The fund is established under Chapter 3 Part 3.6 Division 2 of the *Legal Profession Act* 2007 (Qld) ("LPA"). It is vested in and managed by the Law Society as a source of compensation for pecuniary loss from defaults by law practices. It chiefly consists of contributions or levies paid by legal practitioners and interest from investments.

[9] A default relevantly means either a dishonest failure to pay or deliver money or property (for example, bank credits) received in the course of legal practice or a fraudulent dealing with trust property arising from dishonest conduct.[2]

[10] Pecuniary loss in relation to a default is:

a) the amount of trust money or property not paid or delivered; or

b) the dollar value of a claimant's loss as a result of the default.[3]

[11] Pecuniary loss is not in issue. The applicant bears the onus of establishing "default". To succeed, he has the task of reasonably satisfying the Tribunal of the validity of the trust's claim the applicant must prove that:

(1) the total amount was lost as a result of either misuse of trust money received in the ordinary course of legal practice or a fraudulent dealing by the practice; and

(2) that the money is not "reasonably recoverable from other sources."[4]

[12] The Society submits that the "mortgage financing" exclusions in sub-section 373(1)(b) of the LPA apply to both claims. Mortgage financing is defined in Schedule 2 of the LPA as including facilitating a loan secured or intended to be secured by mortgage by acting as a go-between matching a prospective borrowers and lenders or arranging a loan but excludes preparing the loan instrument.

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1 [2012] QSC 312.
2 *Legal Profession Act* 2007 (Qld) ("LPA") s 356.
3 Ibid s 356.
4 Ibid s 392(a).

[13] A Queensland solicitor must not conduct and manage investment scheme or engage in mortgage financing as part of their law practice under the *Australian Solicitors Conduct Rules* 2012 ("ASCR"), except under a scheme administered by the relevant professional body and where no claim may be made against a fidelity fund.[5]

[14] On the Society's case, the activity of "mortgage financing" cannot be conducted in Queensland in the ordinary course of business because it does not administer any scheme required by the ASCR. On this basis the applicant's deposits could not have been held by the law practice in the ordinary course of legal business.

[15] The application will fail if the Society demonstrates that the default was connected with mortgage financing or an investment purpose.[6]

The review process

[16] The Tribunal's review jurisdiction derives from both the LPA[7] and the *Queensland Civil and Administration Tribunal Act* 2009 (Qld) ("QCAT Act").[8]

[17] Its function is to make up its own mind and reach its own conclusions on the best available information consistently with the powers conferred and corresponding duties imposed by the QCAT Act and the LPA rather than merely testing the legal correctness of the original decision as on appeal in the strict sense.

[18] The intended purpose of a review is to produce the correct and (or) preferable decision.[9]

[19] In performing its role the Tribunal conducts a rehearing on the merits,[10] regardless of process or reasoning error.

[20] The reviewable decision is not presumed to be correct unless the contrary is proved and there is no restriction on the information the Tribunal may consider. Indeed, under s 28 of the QCAT Act, it may inform itself of all relevant material and determined in any appropriate way without the usual strictures of the rules of evidence and common law court practices and customs. For this purpose, the procedure is at the Tribunal's discretion,[11] subject to any mandatory legal rule and the provisions of Chapter 2 Part 3 Division 3 of the LPA.

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5 *Australian Solicitors Conduct Rules* 2012 ("ASCR") r 41.
6 Excluded by LPA s 373(1)(b) or (2).
7 LPA s 392(2).
8 *Queensland Civil and Administrative Tribunal Act* 2009 (Qld) ("QCAT Act") ss 9(2)(b), 17(1), 18(1).
9 Ibid s 20(1).
10 Ibid s 20(2).
11 Ibid ss 28(1), 161.

[21] The suite of orders available to the Tribunal in deciding review proceedings are stated in s 24 of the QCAT Act.

[22] The credibility of witnesses is decisive in relation to the "mortgage financing" exclusion[12] which hinges on whether the applicant agreed to provide a loan facility to either the Kopps or Ms Rong as borrowers at their request. The suggested flaws in the versions of applicant and Leach are identified at [27]-[28] of the Society's outline of submissions filed 28 January 2016.

[23] The applicant maintains that he is telling the truth and that (despite his admitted credibility weaknesses) so is Leach, at least, about the circumstances of the loans.

The hearing

[24] The Society was represented by its experienced general counsel. The applicant is self-representing but has some tertiary level legal education.

[25] The proceedings were conducted over two days and in presenting their cases the parties were permitted to give evidence personally, examine witnesses and make submissions. A "Statement of Agreed Facts" and "Chronology of Events"[13] identify the significant agreed and disputed facts.

[26] The Society relied on affidavit material, documentation and the expert testimony of an accountant to interpret practice and banking records.

[27] The applicant gave evidence himself both by affidavit and orally on affirmation. He also called two witnesses including the principal of the law practice. The Tribunal also examined the applicant and the parties' witnesses under s 98 of the QCAT Act.[14]

The Rong loan

[28] The applicant swears that he met Xu Rong independently of Leach and that the lawyer's only role in the matter was to draft loan documentation and security. Leach denied any involvement in the initial contact or loan negotiations between the applicant and Ms Rong.

[29] There is no dispute that the amount of $150,000 was deposited to the Gateway Lawyers Trust Account on 6 November 2009. It was receipted to a ledger in the name of "Warwick Leonard De Graff". Within the space of a month, $104,000 was diverted to the law practice's general account, with the balance of $46,000 to a company in the United States. The source of the funds was a company business, Jam Hair Salon, controlled by the applicant's former partner, Kirsty Marks.

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12 *De Simone v Victorian Legal Services Board (Ruling No. 3)* [2015] VSC 451 [4].

13 Both filed 19 October 2015.

14 QCAT Act ss 2,3,4,28,29 and 162.

[30] The applicant submits that the only probable conclusion to be drawn from the totality of the evidence is that he gave instructions for the $150,000 not to be released to Rong until the mortgage documents were lodged and that his instructions were disobeyed.

[31] Based on the information of banking records and relevant email exchanges, the Society's investigation report (dated 18 February 2015) concluded that the Rong loan was a sham designed to put the principal of the law practice in funds for personal drawings.

[32] No loan agreement or mortgage documents have ever been produced. The applicant "at last report cannot locate" the alleged borrower.

[33] The Society contends that this limb of the claim must be dismissed as a matter of law because the principal amount was transferred without any legal right or authority from the credit balance of the bank account of a deregistered company the applicant was neither a director nor shareholder of, but in reality probably controlled.

[34] The reason why the claim is said to be doomed is that on Jam Hair Salon's deregistration, its assets (including bank funds) either vested in ASIC by virtue of s 61AD(2) of the *Corporations Act* 2001 (Cth) or, if the property was held in trust, in the Commonwealth under sub-section 61AD(1A).

[35] Consequently, any amount the company owed to the applicant or his family trust for "the money he put into that salon" was not the sort of loss to the fidelity fund is liable for.

[36] At T 1-26 LL 1-8 the applicant swore to an honest claim of right to the $150,000 allegedly constituting the Rong loan based on the fact that he treated Jam Hair as one of his own companies and it owed is family trust at least the claimed amount for sunk costs that is, on to pay down an alleged debt.

[37] The applicant asserts that he did not know at the time he lodged the claim that the company was deregistered. It is now registered with ASIC, having been reinstated on 24 February 2016. He relies on s 601AH(5) of the *Corporations Act* as answering the respondent's argument as to his alleged lack of standing to maintain a claim on the fidelity fund.

[38] That provision provides that if a company is reinstated it is taken to have continued in existence as if it had never been deregistered and any property still vested in the Commonwealth or ASIC re-vests in the company.

[39] The applicant tendered an affidavit from Ms Marks after the hearing had finished, deposing to having authorised the deposit to Gateway Lawyers Trust account on 6 November 2009 and confirming the applicant's entitlement "to utilise the proceeds of that deposit on behalf of a trust associated with him". There is no evidence of service of the affidavit on

the respondent. However, the applicant relies on s 28(3) of the QCAT Act as justifying late reception. He says, in effect, that the material is necessary for the Tribunal to decide the proceedings on the full facts.

[40] The Society does not object to the late filing of Ms Marks' evidence and concedes that Jam Hair's company registration was reinstated on 24 February 2016 but denies that without a court order under s 601AH(3)(c) – of which there is no evidence – that this has the effect of retrospectively validating transactions during the period of deregistration and the re-vesting of property is wholly prospective.

[41] Thus, in the Society's submission, Ms Marks had no power to authorise the applicants dealing with the $150,000 on 6 November 2009 because at that time it was legally owned by either the Commonwealth or ASIC. Assuming that Jam Hair did owe his family trust $150,000, any provable loss is claimable against the property vested in ASIC, not the fidelity fund.

[42] I agree with the Society's analysis of the legal position. The applicant has not made out any valid legal right as trustee or beneficiary to transfer funds vested by statute in ASIC to his family trust. Accordingly, assuming the deregistered company was indebted to the applicant's family trust to the tune of $150,000 as at 6 November 2009, it could not discharge it via the third party deposit to the law practices accounts.

[43] Even if I am wrong about that, for the reasons that follow, the applicant has failed to satisfy me that the $150,000 was transferred as a loan to Ms Rong at her direct request to finance a soft drink factory. This finding makes deregistration a moot point.

The Kopp loan

[44] The applicant claims to have met Brian Kopp in a hotel, where the matter of the loan in dispute was first discussed. This meeting is denied by Brian Kopp. The applicant suggests that if it wasn't actually Brian Kopp he met then it was "someone pretending" to be him.

[45] The Kopps disavow borrowing money from the applicant or the law practice. They say they had never even heard of him until 13 June 2013 when a letter was received from him acknowledging payment of principal and interest but demanding $4,929.47 in penalty interest on late payments.

[46] They deny ever making any interest payments to him. Their evidence is supported by Exhibit GAF1 which shows that the money was deposited into Leach's general account and never made its way to the Kopps.

[47] Leach also denies putting Brian Kopp and the applicant into contact with each other or procuring the applicant to deposit any money into his practice accounts for on lending purposes.

[48] A loan agreement dated 27 May 2010 between the applicant as trustee (for the Darrell Featherstone Family Trust No. 2) and Brian and Carolyn Kopp as joint borrowers and a Form 2 mortgage purportedly signed on 17 May 2010 by the Kopps and witnessed by a commissioner of declarations (document number 3 of the trial reference bundle at page 109) are relied on as confirming the regularity of the loan.

[49] The applicants' signature on the loan agreement is witnessed by Mark Surman (another of the law firm's clients). Leach ostensibly witnessed the Kopps'. The Form 2 was signed by the applicant and witnessed by Leach on 19 May 2010. The Kopps say the documents are forged using legitimate loan documents they had signed when Leach acted for them previously in a legitimate loan transaction.

[50] A letter "of demand" allegedly written by the applicant to Mrs Kopp was produced in evidence in circumstantial proof of the alleged loan transaction (page 159 of the trial reference bundle dated 13 June 2013). The applicant denies writing this letter. Both he and the Kopps accuse Leach of fabricating it in an attempt to extract money from the Kopps to assist in repaying the applicant. Alternatively, the applicant suggests Mr Kopp manufactured the letter to defuse the concern that he had borrowed $50,000 without telling him, or suggests as another possible logical inference that the document was most likely pieced together by Leach or the Kopps and that the interest repayments were probably made by Leach to cover up his deception.

[51] On 21 March 2013 the claim in respect of the Kopp loan was withdrawn by email. It was reinstated on 21 June 2014 after the applicant claimed to have discovered that Mr Kopp and Leach were long time business partners.

[52] A form attached to the letter of demand states that "$50,000 being the capital of the loan was repaid to me by direct deposit on 27/3/13". The writing is the applicant's but I find it relates to a different $50,000 amount paid to him by Leach on 27 March 2013 for rental arrears, in exchange for the withdrawal of the claim against the Kopps.

[53] Leach admitted to paying the applicant sums of money from time to time in the context of questioning about the interest repayments on the Kopp loan but denied any knowledge of the repayment of interest on the alleged Kopp loan but later said of the interest schedule attached to the letter dated 13 June 2013 to Mrs Kopp "… he didn't know what the summary of the interest was or where it came from but certainly he was "doing everything (he) could to keep (the applicant) appeased".

Leach's creditworthiness

[54] Leach has serious credibility problems. He conceded acting dishonestly over a long period time and misappropriating client's funds and lying to cover it up. In explaining the Form 2 in relation to the purported loan to Rong, he said he would have done that to make it look as though the

applicant's instructions were being followed. As to other aspects of his conduct he claimed privilege against self-incrimination. No inference for or against the applicant is made solely based on Leach's reliance on his substantive common law rights, which are not diminished in Tribunal proceedings because of the rules of evidence exception.

[55] The applicant objects to the admission of Leach's involvement in similar bogus loan transactions with other clients (e.g. Peter Mallan, John Farrer, the De Graff estate and Mark Surman) as "extraneous to the facts" to the disputed circumstances of the loans to Rong and the Kopps.

[56] In my view, however, the "previous alleged loans" are circumstantially probative of Leach's *modus operandi*. Just because his probable conduct in those transactions is more consistent with the Society's case than the applicant's does not mean, of course, that the applicant is lying or that because he has done it before Leach has done it again here. It does, however, help to contextualise the disputed loans and resolve factual discrepancies.

[57] In civil litigation, as opposed to criminal proceedings, there is no specific rule as to the admission of what might be similar fact evidence and even if there was, the Tribunal is not bound by it. The question is one of relevance and cogency.[15]

[58] There is no unfairness in using this evidence given the applicant had notice of it. The evidence is directly relevant to the existence of a fact in issue; namely, the circumstances of the Rong and Kopp loans. It is persuasive and supports that the Society's submissions as to the facts of that issue be accepted.

[59] The De Graff evidence is suggestive of the $150,000 deposit on account of "the Rong loan" being siphoned off by Leach to reimburse the estate $140,000 he had misappropriated from it in late October 2009.

[60] It is highly improbable that Leach would use the deposit in this way if there really was a loan agreement under which Rong was actually expecting to be put into funds of $150,000. It is much more consistent with mortgage financing where there is no specific client expecting money to be advanced.

[61] The Farrer evidence also lends considerable weight to the Society's case. It concerns other loans arranged by Leach to Rong, the same person with

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15 See *Mood Music Publishing Co Ltd v De Wolfe Ltd* [1977] 1 All ER 767, 766; *Sheldon v Sun Alliance Australia Ltd* (1989) 53 SASR 97, 145-148; *Edwards v Clinical Beauty Pty Ltd v Chan* [2002] QDC 28 [5]; *Kation Pty Ltd v Lamiru Pty Ltd (No 2)* [2009] NSWCA 428 [10]. See also "Similar Fact Evidence in Civil Proceedings: Proof or Policy", (2006) 26 University of Queensland Law Journal 99 and "Does the Similar Fact Evidence Rule Apply in Civil Cases – *Sheldon v Sun Alliance Ltd*" (1991) 13 Sydney Law Review 620.

whom the applicant alleges he independently agreed to lend $150,000. The evidence is of loans of $150,000 ostensibly to Rong. The prospect of making each of those loans were presented by Leach to Farrer. The loans were to be secured by mortgage. Farrer never met Rong. There were two loans, Farrer received repayment of one, and his money on the second was put to meet defalcation by Leach against the de Graff estate (see Exhibit GAF33 – to the First Affidavit of Forster).

[62] The Surman evidence shows that Leach was desperately trying to repay the applicant by borrowing $200,000 from Surman on the pretext it was for the Kopps but Surman was only interested in advancing $50,000 which Leach agreed to secure with his personal guarantee of repayment plus $10,000 by the end of 2015.

[63] The combined effect of the pattern of conduct tends inferentially to evidence that, contrary to the applicant's case of agreeing to lend to Rong during a meeting between the two, Leach probably approached the applicant with a sham "mortgage financing" proposal to defraud him.

[64] The applicant deposes at [1] of his statutory declaration of 18 June 2012 that he was told by Leach that contact had been made by (the Kopps) and the matter proceeded". In due course he was advised that the documents "were done" and all that was required was for the money to be transferred to his trust account so it could be given to the client. However, the applicant would have already known the documents were done, because he signed them prior to depositing any money into Gateway Lawyers' Trust Account on 31 May and 1 and 2 June 2010.

[65] A telling circumstance is that genuine borrowers would have been making enquiries about those expected funds (especially after having signed a loan agreement and mortgage document) or complaining about having to pay interest for a loan they did not get the benefit of because of Leach's dishonesty. But there was no such contact by either in this case.

Against this background I make the following findings of fact:

- Rong did not request a loan of $150,000 for a soft drink business from the applicant. It is more likely Leach devised the scheme and then induced the applicant to enter into it without Rong knowing anything about it.

- Based on inferences from the law practice's books, the Rong loan was arranged by Leach without any contact between the applicant as lender and Rong as borrower.

- Likewise, neither of the Kopps asked the applicant to lend nor received the disputed $50,000, despite Leach assuring the applicant otherwise. Brian Kopp did not meet the applicant at a hotel or ask for a loan of $50,000. Nor was there was any such meeting with any other person passing himself off as Mr Kopp as the applicant claims as a logical possibility.

- Leach probably fabricated the letter dated 13 June 2013 to Mrs Kopp in an attempt extort money from them to repay the applicant. The applicant admits he gave the bottom third of the last attachment to that letter to Leach and alleges that Mr Kopp somehow obtained the bottom third and fabricated a composite document. This theory is not supported by Leach. There is no logical explanation for the Kopps fabricating the letter of 13 May.

[66] On the basis of these findings, the Society has made out the "mortgage financing" exception. Leach was undoubtedly arranging fake loans on behalf of real clients for his own purposes and the applicant may well be an innocent victim of a sham investment scheme but cannot legitimately recoup his loss from the fund.

[67] Accordingly, the reviewable decision is confirmed without variation.