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The Supreme Court of Canada Speaks on Lawyers' Conflicts of Interest

by
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I Introduction

On December 20, 1990 the Supreme Court of Canada released its reasons for judgment in *Martin* v. *Gray*, reported at (1991), 121 N.R. 1. The Supreme Court disqualified the defendant's lawyers from continuing to act for the defendant on the basis of a so-called "former client" conflict of interest. It is the first Supreme Court decision which directly considers the circumstances in which a conflict of interest in the representation of clients in litigation can lead to a disqualification of counsel.

The case ought to be compulsory reading for every practising lawyer in Canada. For those who have not yet seen and digested the full reported decision this is intended to be a synopsis of the case, coupled with a series of implications or potential implications for lawyers and law societies.

II The Circumstances in *Martin* v. *Gray*

These were the circumstances of *Martin* v. *Gray*. In 1983 in Winnipeg a lawyer, Twaddle, began acting for Martin in litigation against Gray, the administrator of the estate of a John Edwin Macdonald. Dangerfield, an articled clerk and subsequently a lawyer, acted in association with Twaddle on behalf of Martin. Dangerfield was actively involved in the representation of Martin in the litigation, including settlement discussions with lawyers for Gray. Dangerfield was privy to many confidences of the client. Susequently, Twaddle was appointed to the bench and Dangerfield joined another firm. Her original law firm continued to represent Martin.

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remaining assets of the estate were $100,000 being held by the Trustee in Bankruptcy and a $1.89 million judgement against the applicant-widow. *Held*, for the trust company, that where there exists a potential for litigation between the executor and the estate, the executor cannot instruct counsel on two sides of the issue and should step aside or be removed. The Court denied the application of the widow. The court noted that the allegations that the trust company failed to communicate fully with the applicant-widow, and the disagreement between the two executors were not sufficient for removal.

WILLS AND ESTATES - Interpretation - no errors of law

Kutnik et al. v. *Yelenich Estate et al.*, S.C.A. 02363, Clarke, C.J.N.S., 19 April 1991. **S310/19**

WILLS AND ESTATES - Valuation of goods devised - machine shop tools

Doucette v. *Doucette Estate*, S.Y. 1610, Haliburton, L.J.S.C., 6 May 1991. **S309/19**

The Supreme Court of Canada Speaks on Lawyers' Conflicts of Interest

Continued

Gray was represented throughout by the Thompson firm. In 1987 Dangerfield's firm merged with the Thompson firm.

The lawyers for Gray brought an application for a declaration that the Thompson firm be disqualified from acting on behalf of Martin in the proceedings because of Dangerfield's membership in the Thompson firm.

In the court proceedings in Manitoba Dangerfield and members of the Thompson firm swore affidavits and gave undertakings to the effect that the case had not been discussed between Dangerfield and the lawyers working on the case and that no discussions would take place in the future. (In fact, Dangerfield and the firm undertook that Dangerfield would work only at home and not in the office at all until the litigation in the case had been concluded.)

The Supreme Court of Canada ruled unanimously that the Thompson firm must be disqualified from acting for Martin in the litigation. The Court announced its decision in May of 1990. These reasons were released on December 20, 1990.

III The Supreme Court Decision

Mr. Justice Sopinka wrote the majority decision in the case, concurred in by three other justices. Mr. Justice Cory delivered concurring reasons of himself and two other justices which are highly critical of the majority decision.

Mr. Justice Sopinka's decision has six components. The first is an isolation of the values or principles at stake in cases involving lawyers' conflict of interest. Second are the policy considerations behind these principles - what he refers to as considerations of legal ethics. Third is his review of the evolving law on disqualifying conflicts of interest in England, Australia, New Zealand, the United States and Canada. Fourth, and by reference to the competing principles, is an articulation of the appropriate test to be applied in cases of disqualifying conflict of interest. Fifth is the learned judge's application of this test to the circumstances in *Martin* v. *Gray*. Sixth is his invitation to the legal profession to reconsider the ethical rules relating to conflict of interest with a view to developing or approving of "institutional devices" which might moderate the rigour of the test he applies in the case.

1. *The Values and Principles at Stake*

Mr. Justice Sopinka articulated three values which arise when a party seeks to disqualify the opponent's lawyer on the basis of a conflict of interest. He described these values in this way, at p. 8:

> There is first of all the concern to maintain the high standards of the legal profession and the integrity of our system of justice. Furthermore, there is the countervailing value that a litigant should not be deprived of his or her choice of counsel without good cause. Finally, there is the desirability of permitting reasonable mobility in the legal profession.

In examining the way in which these principles are fitted into the relationship between lawyer and client, Mr. Justice Sopinka noted that the central feature of client representation by lawyers is the lawyer's commitment to maintain the confidences and secrets of the client. In general he embraced the importance of this value, noting that the law itself protects confidential communications, "perhaps unduly". This commitment takes on particular importance in the context of litigation. He stated at p. 9:

> Clients [bare their souls] in the justifiable belief that nothing they say will be used against them and to the advantage of the adversary. Loss of this confidence would deliver a serious blow to the integrity of the profession and to the public's confidence in the administration of justice.

2. *Legal Ethics - Policy Considerations*

Mr. Justice Sopinka found these values to be fully articulated in the codes of professional conduct for lawyers. While he noted the difference between ethical rules and legal rules governing conflicts of interest, he relied substantially on the provisions of codes of ethics in his analysis. The codes call for a high standard of commitment on the part of lawyers to avoid conflicts of interest which could be perceived to jeopardize the client's confidences. This approach forms the base upon which the learned judge constructs the legal standard for a disqualifying conflict of interest. In particular, he quoted the Canadian Bar Association's Code of Professional Conduct (1974), Chapter V Rule and Commentaries 11 and 12. The Rule states:

> The lawyer must not advise or represent both sides of a dispute and, save after adequate disclosure to and with the consent of the client or prospective client concerned, he should not act or continue to act in a matter when there is or there is likely to be a conflicting interest. **A conflicting interest is one which would be likely to affect adversely the judgment of the lawyer on behalf of or his loyalty to a client or prospective client or which the lawyer might be prompted to prefer to the interests of a client or prospective client.** (My emphasis.)

Mr. Justice Sopinka also emphasized the significance of Commentaries 11 and 12. Commentary 11 establishes the ethical rules in the so-called "former client" conflict scenario. It provides:

> 11. A lawyer who has acted for a client in a matter should not thereafter act against him (or against persons who were involved in or associated with him in that matter) in the same or any related matter, **or place himself in a position where he might be tempted or appear to be tempted** to breach the Rule relating to Confidential Information. It is not, however, improper for the lawyer to act against a former client in a fresh and independent matter wholly unrelated to any work he has previously done for that person. (My emphasis.)

This provision introduces the concept that the disqualification extends the ethical proscription to proceedings against a former client in "the same or any related matter". This is the so-called "substantial relationship" test. As well, the highlighted part of Commentary 11 underscores the importance of perception of impropriety when it comes to confidential information. The lawyer must not allow himself or herself to be tempted **or appear to be tempted** to disclose confidential information. This is the "appearance of impropriety" test.

The final provision of the CBA Code which Mr. Justice Sopinka referred to, Commentary 12, addresses the scope of the definition of "lawyer" for the purposes of conflicts of interest. Commentary 12 provides:

> 12. For the sake of clarity the foregoing paragraphs are expressed in terms of the individual lawyer and his client. However, it will be appreciated that the term "client" includes a client of the law firm of which the lawyer is a partner or associate whether or not he handles the client's work.

This commentary sets out the principle upon which the knowledge of one lawyer concerning the affairs of a client is imputed to all of the lawyers in the firm.

Mr. Justice Sopinka stated at p. 11 that these statements should be accepted as

> the expression by the profession in Canada that it wishes to impose a very high standard on a lawyer who finds himself or herself in a position where confidential information may be used against a former client. The statement [in the Code] reflects the principle that has been accepted by the profession that even an appearance of impropriety should be avoided.

3. *The Law on Disqualifying Conflict of Interest*

Following an extensive review of the various authorities in common law jurisdictions around the world, the learned judge identified two basic approaches to disqualifying conflicts of interest. The older, more traditional, test from the older English case of *Rakusen* v. *Ellis, Munday and Clarke* is that there must be "the probability of real mischief". The second, newer and more stringent, approach is "the possibility of real mischief". This test originated in the United States in the 1950s. In his review Mr. Justice Sopinka concluded that there had been a noticeable movement toward the second more stringent test in Canada, though there has been great diversity on this question in the different provinces.

4. *The Test for Disqualifying Conflict of Interest*

Ultimately, he concluded that the older "probability of real mischief" test was not sufficiently high to satisfy the public requirement that there be an appearance of justice. Specifically, he pointed out that violations of confidentiality were not usually susceptible of proof. A more invasive test was required. He said at pp. 29-30:

> Since, however, it is not susceptible of proof, the test must be such that the public represented by the reasonably informed person would be satisfied that no use of confidential information would occur. That, in my opinion, is the overriding policy that applies and must inform the court in answering the question: Is there a disqualifying conflict of interest? In this regard, it must be stressed that this conclusion is predicated on the fact that the client does not consent to but is objecting to the retainer which gives rise to the alleged conflict.

It was recognized by the Court that two facts must exist in such situations. The first is that the lawyer must have received confidential information. Second, there must be a risk that in the subsequent representation such information will be used to the prejudice of the client. However, serious problems arise in considering how to prove or disprove these facts. With respect to the question of receipt of confidential information, Mr. Justice Sopinka concluded that lawyers should bear a heavy onus of establishing that confidential information had not been communicated. There is, then, a **rebuttable** presumption that confidential information was communicated to the lawyer. While the rebuttability of this presumption may be difficult, the learned judge recognized that this was a less demanding standard than the approach in the United States where this presumption is irrebuttable.

As to the second issue, the risk of prejudicial use of the information, Mr. Justice Sopinka recognized that the likelihood of such use is related to the degree to which it was realistic to apply the assumption of "imputed knowledge". That is, where one member of a firm is in possession of confidential information, the whole firm is deemed to know that information regardless of the size of the firm or the way in which it is organized. In the learned judge's view this is particularly troublesome in cases where a lawyer with only "imputed" knowledge joins another firm where his "imputed" knowledge infects, through imputation, all of the lawyers in the new firm. He regarded disqualification in such situations as "unrealistic in the era of the mega-firm" and "overkill".

5. *Law Society Reconsideration of Ethical Rules*

This led Mr. Justice Sopinka to a discussion of

"institutional mechanisms" which might moderate the rigour of the imputation doctrines. Such mechanisms, he suggests, might include "Chinese walls" and "cones of silence". Notwithstanding his belief in the possibility that such mechanisms might effectively insulate the "infected" lawyer and ensure that confidences are preserved, the learned judge was unwilling to sanction their use in the absence of approval by the governing bodies of the profession. He said at p. 32:

> It can be expected that the Canadian Bar Association, which took the lead in adopting a Code of Professional Conduct in 1974, will again take the lead to determine whether institutional devices are effective and develop standards for the use of institutional devices which will be uniform throughout Canada. Although I am not prepared to say that a court should never accept these devices as sufficient evidence of effective screening until the governing bodies have approved them and adopted rules with respect to their operation, I would not foresee a court doing so except in exceptional circumstances. Thus, in the vast majority of cases, the courts are unlikely to accept the effectiveness of these devices until the profession, through its governing body, has studied the matter and determined whether there are institutional guarantees that will satisfy the need to maintain confidence in the integrity of the profession.

6. *The Outcome in the Case*

Given the high standard set by the majority of the Court, and given the absence of any "institutional mechanisms" approved by the Law Society of Manitoba at the time of the case (or applied by the Thompson firm from the time when Dangerfield joined the firm) it was clear that the Thompson firm would be required to be disqualified for acting for Gray. Mr. Justice Sopinka so held.

7. *Mr. Justice Cory's "Dissenting" Concurrence*

Mr. Justice Cory expressed animated dissent from the test articulated by Mr. Justice Sopinka. In particular, he took issue with the weight which the majority assigned to the values of client choice and lawyer mobility as moderators of the more general, and in Mr. Justice Cory's view fundamentally important, value of the maintenance and integrity of our system of justice. Mr. Justice Cory's view was that the integrity of the administration of justice ought not to be compromised to accommodate the interests of lawyers in mega-firms and their corporate clients. He was skeptical of the suggested institutional mechanisms. He presented a litany of opportunities for client confidences to be revealed advertently or inadvertently. In a sharply worded critique of the Sopinka "mega-firm" orientation, he reviewed the statistics on the concentration of lawyers in Ontario, noting that in 1990 64.3% of lawyers there still practice in firms of 10 lawyers or fewer in size. He concluded this part by saying at p. 42:

> This indicates that, although the large firms may be the movers and shakers on Bay Street, they do not represent the majority of lawyers soldiering on in the cause of justice.

He would have had the Court take this approach (at p. 42):

> The judicial system and the confidence of the public in its operation are too important to be put at risk by any appearance of unfairness. Unfortunately, no matter how scrupulously ethical an individual lawyer or firm may be, the appearance of unfairness will always be present when, as in this case, one or more lawyers who had a substantial relationship with a client become members of a firm acting for an opposing party. The opportunities for disclosure, even of an inadvertent nature, are too frequent and the possibility of discovering such disclosures too minimal to permit anything less than an irrebuttable presumption that the knowledge of one member of a law firm constitutes the knowledge of all of the lawyers in that firm. Only such a test will ensure the public's confidence in the administration of justice.

IV Implications

1. *A New Conflict of Interest Rule for Nova Scotia?*

It is fairly obvious that the Supreme Court of Canada has articulated a tougher standard regarding lawyer conflict of interest than many lawyers considered previously to

be the law or to be appropriate. In some respects this appears to be inaccurate, at least for Nova Scotia. Since the Appeal Division's decision in *Fisher* v. *Fisher* (1986), 76 N.S.R. (2d) 326, it is possible that the standard described by the Supreme Court, based upon appearances of impropriety and a virtually irrebuttable presumption of imputed knowledge, has been the law in Nova Scotia. Indeed, the Supreme Court refers to *Fisher* v. *Fisher* as an example of the stricter "appearances" standard in which lawyer assurances (to rebut the imputation of knowledge) were not accepted by the Court. So it could be that the Supreme Court has done no more, from a Nova Scotia perspective, than bring a number of jurisdictions up to the Nova Scotia standard.

2. *The Nova Scotia Professional Conduct Handbook and Martin v. Gray*

One question not addressed in the discussion of the case is the degree to which recently developed provincial codes of ethics have deviated from the 1974 CBA *Code of Professional Conduct*, and whether such deviations make any difference in the world of disqualifying conflicts of interest. The *Nova Scotia Legal Ethics and Professional Conduct Handbook* tracks closely the 1974 and 1987 CBA Codes, and it is likely that the present state of the Nova Scotia law on disqualifying conflicts of interest, to the extent that it is based upon what the Handbook proscribes, is exactly as the Supreme Court has stated. It is not clear in any event, despite extensive reference to the 1974 CBA Code, that codes of ethics are as big a factor in establishing the basic principles as even Mr. Justice Sopinka suggests. This is because the 1974 CBA Code of Professional Conduct has itself been superceded by the 1987 Code. Curiously, the Court made no reference to the 1987 document.

3. *A Canada-Wide Rule*

One consequence of the decision is that the standard for disqualifying conflict of interest will, at least temporarily, be consistent across the country. This is probably fortunate in these days of national (and international) law firms. In this respect the Supreme Court has, almost without realizing it, temporarily enjoined one aspect of the provincial balkanization of legal ethics in Canada.

4. *Mergers and Taking on New Lawyers*

Another practical consequence is that those law firms who have not previously done so will have to be very much more vigilant in screening out possible conflicts when they take on lawyers from other firms or when law firms merge. The implications could be substantial. For example, it is reasonable to speculate that in some cases the value to a law firm of the retention of a client otherwise lost due to a disqualifying conflict of interest may outweigh the value of the new lawyer (the "Typhoid Gerry" who creates the disqualifying conflict of interest) to the firm.

5. *The Unanswered Question - "Double Imputation"*

In both the Sopinka and Cory judgments the "double imputation" scenario is left undecided. "Double imputation" arises where a lawyer, not involved in the representation of a client of his or her firm - Client A - (but who is by law and ethics saddled with the imputed knowledge of the client's confidences), leaves the firm and joins the law firm which represents the first client's adversary - Client B. Even though the lawyer in question does not represent Client B, his or her imputed knowledge, if imputed to the rest of his or her associates at the new firm, would have the effect of disqualifying the whole firm from continuing its representation of Client B. This reach to the disqualification rule would exponentially increase the problems for identifying the conflicts of interest which "Typhoid Gerry" would bring to the new firm, since it would require the new firm to review not only the potential conflicts of interest generated by Gerry's former clients but also all of the conflicts generated by all of the clients in Gerry's former law firm. The implications for the principles of client choice of counsel and lawyer mobility are very substantial. It is not surprising, therefore, that even Mr. Justice Cory, whose judgment strongly embraced principle over pragmatism, indicated that this "double imputation" scenario "be left for another occasion".

6. *Law Society Approval of Institutional Mechanisms*

Finally, there remains the question of whether law societies should develop and sanction "institutional mechanisms" which would allow law firms to avoid the consequences of *Martin* v. *Gray*. The Canadian Bar Association has struck a special committee to consider

the question. The Legal Ethics Committee of the Nova Scotia Barristers' Society has recently considered the question and recommended to the Council of the Society that "institutional mechanisms" not be developed or approved by the Society and that the Professional Conduct Handbook not be amended to introduce such accommodations. The Committee recommended that the dilemma of "double imputation", left open by the Supreme Court, should be addressed in the courts rather than by a set of rules introduced by law societies. Bar Council has not yet decided upon the recommendations of the Committee and will be addressing these issues prior to the CBA Annual Meeting in August of this year. It will obviously be important to monitor developments in the courts and in other law societies to observe whether the Supreme Court decision in *Martin* v. *Gray* has not started a new round of balkanized legal ethics, this time having raised the balkanization to the level of rules of law.

Ideas for this article were contributed by Professor Archie Kaiser, Rick Southcott and Susan MacKay.

Instrument of Subdivision

by
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For the past three years, fourteen rural municipalities in Nova Scotia have been using Instrument of Subdivision. This procedure was introduced as a replacement for the infamous "four lot rule" through revisions to the *Planning Act* in 1987. Instrument of Subdivision provides for subdivision approval of lots without the usual formalities. Title is assured for subdivisions of this nature insomuch as compliance with the *Planning Act* is concerned.

The basic underlying principal behind Instrument of Subdivision and its predecessor the four lot rule, is not without merit. They were both designed to facilitate the occasional single lot transfer between family members and neighbours in rural communities. They are based on the premise that people in low value, slow growth areas of the province should be offered some relief from the onerous subdivision process.

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We should indeed give the rural property owner every consideration, provided of course, that any such benefit to this particular group is not detrimental to any other members of society or to the long term development of the province. In particular, we must weigh the short term benefit to the land owner/developer against the added costs and risks to subsequent owners and adjoiners.

The four lot rule was far from perfect, but it did accomplish its objective in exempting a minimal amount of subdivision activity from the rules. The major problem that led to its downfall was the difficulty of interpreting the wording of the rule. Lawyers, in particular, found the wording ambiguous and often disagreed with each other as to whether the remnant parcel formed the fourth lot. There was also the question of whether a newly created lot could then be further subdivided into four new lots using this rule. Since there was no requirement to record this subdivision activity, searching was difficult at best.

Good title to a property depends on compliance with prevailing legislation. It was often difficult however, to determine if an unapproved lot had truly qualified for the four lot rule exemptions. In response to this expanding problem, legislators changed the *Planning Act*, did away