IN THE COURT OF APPEAL OF NEW ZEALAND

CA191/2012
CA194/2012
CA201/2012
CA204/2012
[2013] NZCA 188

BETWEEN	WILLIAM PATRICK JEFFRIES MICHAEL HOWARD REEVES DOUGLAS ARTHUR MONTROSE GRAHAM LAWRENCE ROLAND VALPY BRYANT Appellants
AND	THE QUEEN Respondent

CA225/2012
CA226/2012
CA227/2012
CA228/2012

BETWEEN	THE QUEEN Appellant
AND	WILLIAM PATRICK JEFFRIES MICHAEL HOWARD REEVES DOUGLAS ARTHUR MONTROSE GRAHAM LAWRENCE ROLAND VALPY BRYANT Respondents

Hearing:	4–7 March 2013
Court:	Randerson, Wild and French JJ
Counsel:	J A Farmer QC, M A Corlett, D H O'Leary and M A Sissons for Jeffries, Reeves, Graham and Bryant C R Carruthers QC and D R La Hood for the Crown
Judgment:	30 May 2013 at 10:00am

JUDGMENT OF THE COURT

A **The appeals against conviction (CA191/2012, CA194/2012, CA201/2012 and CA204/2012) are dismissed.**

B **Leave to appeal is granted to the Solicitor-General in respect of appeals CA225/2012, CA226/2012, CA227/2012 and CA228/2012 but a final decision on those appeals is deferred until we have the further reports identified in C below.**

C **We direct that updated reports be provided to this Court as soon as possible for each of the respondents under s 26A of the Sentencing Act 2002, solely to confirm the availability of suitable addresses for home detention in combination with sentences of community work.**

D **The sentences of reparation imposed on Douglas Arthur Montrose Graham and Lawrence Roland Valpy Bryant remain in place.**

REASONS OF THE COURT

(Given by Randerson J)

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Introduction

[1] The appellants appeal against conviction on charges laid under s 58(3) of the Securities Act 1978 arising from the financial collapse of Lombard Finance and Investments Ltd in 2008. We will refer to the legislation as the Act and to the company as Lombard. The Solicitor-General seeks leave to appeal against sentences of community work imposed on the appellants.

[2] The appellants were directors of Lombard, a finance company raising money from the public and lending money predominantly to property developers.

[3] During 2006 and 2007 there was a tightening of economic conditions resulting in the collapse of a number of other finance companies. While recognising Lombard was experiencing liquidity issues and taking some steps to address them, the appellants nevertheless formed the view that the company could continue raising funds from the public. On 24 December 2007, the company issued an amended prospectus under the Act. The charges against the appellants arose from the amended prospectus. Lombard's position deteriorated further thereafter and receivers were appointed on 10 April 2008. Investors in the company sustained substantial losses.

The indictment

[4] The indictment contained five counts. Count one alleged that the prospectus included untrue statements in five particular respects. In summary these were:

> (i) The omission of material information relating to adverse liquidity issues including the deterioration in the company's cash position from the balance at 30 September 2007 and the failure to achieve forecast cash receipts and loan repayments.
>
> (ii) The omission of information about adverse impairment and recoverability issues for the loans of Lombard's five major borrower groups.
>
> (iii) Untrue statements in relation to adherence to lending and credit approval policies.

(iv) An untrue statement in an extension certificate that the financial position shown in the prospectus had not materially and adversely changed during the period from the date of the statement of financial position to the date of the certificate.

(v) An untrue statement that there were no other material matters relating to the offer of securities under the prospectus.

[5] To the extent that omissions were alleged, the Crown relied on s 55(a)(ii) of the Act. This provides that a statement in a registered prospectus or advertisement is deemed to be untrue if:

> … [I]t is misleading by reason of the omission of a particular which is material to the statement in the form and context in which it is included: …

[6] Counts two to four in the indictment alleged offending under s 58(1) of the Act.[1] It was said there were untrue statements in advertisements for three other forms of investment: unsecured subordinated notes, unsecured subordinated capital notes and secured debenture stock. Count five related to alleged untrue statements in an advertisement in the form of a DVD.

[7] The appellants were tried by Dobson J sitting without a jury. After a hearing occupying some eight weeks, Dobson J delivered his verdicts on 24 February 2012.[2] He found all the appellants guilty on count one but only in respect of two of the five particulars. These were particular (i) (relating to Lombard's liquidity) and particular (v) (which the Judge saw as merely consequential upon his finding on particular (i)). The appellants were also found guilty on counts two, three and four but only in respect of particular (iii). This alleged an omission to include information relating to Lombard's deteriorating cash position. All appellants were acquitted on count five, the Judge finding that the DVD did not constitute an advertisement within the meaning of the Act and that there was no fault on the part of the appellants.

[8] At trial, the appellants denied making any untrue statements (whether by omission or otherwise). They also relied on s 58(4) of the Act. This provides a defence if the person charged proves that the alleged untrue statement was immaterial or that he or she had reasonable grounds to believe, and did believe, that

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1 This section is set out at [18] below.
2 *R v Graham* [2012] NZHC 265, [2012] NZCCLR 6.

the statement was true. The Judge was not satisfied that any of the appellants had made out the statutory defence.

[9] On 29 March 2012 Dobson J sentenced the appellants as follows:[3]

Mr Jeffries	400 hours community work
Mr Reeves	400 hours community work
Sir Douglas Graham	300 hours community work and reparation of $100,000
Mr Bryant	300 hours community work and reparation of $100,000

[10] The Solicitor-General contends that these sentences are manifestly inadequate. He seeks substituted sentences comprising a combination of home detention and community work.

Scope of the conviction appeals

[11] The scope of the conviction appeals was limited in four respects. First, the verdicts in the High Court meant that the appellants' case was restricted to the finding that the relevant statements were untrue due to material omissions in relation to Lombard's liquidity. Second, the focus of the argument was on the finding on count one relating to the prospectus. Counsel accepted that the outcome of the appeals in relation to counts two, three and four would be determined by the Court's conclusion on count one. Third, counsel did not seek to differentiate between the appellants for the purposes of the conviction appeals. The same arguments were made for all. Fourth, the Crown accepted the Judge's finding that the appellants believed the statements in the amended prospectus were true despite the matters the Crown alleged were omitted.

The grounds for the conviction appeals

[12] The conviction appeals were advanced on four principal grounds:

(a) The Judge misdirected himself on the approach to omissions under s 55 of the Act.

3 *R v Graham* [2012] NZHC 575.

(b) The Judge's conclusion that the statements in the prospectus were untrue was unreasonable or could not be supported having regard to the evidence.

(c) The Judge misdirected himself as to the correct approach to the statutory defence under s 58(4) of the Act.

(d) The Judge's conclusion that the appellants did not establish the defence under s 58(4) was unreasonable and could not be supported having regard to the evidence.

The statutory framework

[13] The Act has been much amended but the provisions we refer to in the analysis that follows were in force at the relevant time and remain substantially unchanged. Part 2 of the Act imposes restrictions on the offer of securities to the public. Where prescribed forms of investments are offered to the public, the offer must be made in, or accompanied by, a registered prospectus that complies with the Act and regulations.[4]

[14] The form and content of the prospectus were prescribed by the Act[5] and at the time by the Securities Regulations 1983.[6] The statutory intention to prohibit false or misleading material in a prospectus is underlined by s 34(1)(b). It provides that:

> (1) No registered prospectus shall be distributed by or on behalf of an issuer, —
>
> …
>
> (b) If it is false or misleading in a material particular by reason of failing to refer, or give proper emphasis, to adverse circumstances (whether or not it became so misleading as a result of a change in circumstances occurring after the date of the prospectus).[7]

[15] An issuer may only rely on a prospectus to allot securities for up to nine months from the end of the period to which audited financial statements accompanying the prospectus relate.[8] In Lombard's case, the last audited financial statements were for the year ended 31 March 2007 and were attached to a prospectus

4 Securities Act 1978, s 33(1)(c).
5 Sections 39–41.
6 Now replaced by the Securities Regulations 2009.
7 The duty not to mislead is underlined in the Securities Regulations 1983, rr 5(1), 8 and 34.
8 Section 37A(1)(c).

Lombard had issued in September 2007. Under the Act, the September prospectus would have expired on 31 December 2007.[9]

[16] However, the life of a prospectus may be extended if the directors certify (within nine months after the date of the financial statements contained in the prospectus) that the company's financial position has not materially and adversely changed from that reflected in the published financial statements. The certificate must state that the registered prospectus is not false or misleading in a material particular by reason of failing to refer, and give emphasis to, adverse circumstances.[10] The Lombard directors took advantage of the opportunity to extend the life of its prospectus beyond 31 December 2007 by completing and lodging with the Companies Office the amended prospectus on 24 December 2007 along with an extension certificate attaching unaudited financial statements for the period ending 30 September 2007.[11]

[17] Issuers of securities are not required to provide a copy of a registered prospectus to every investor. Issuers may instead issue investment statements to provide "certain key information that is likely to assist a prudent but non-expert person to decide whether or not to subscribe for securities".[12] However, if a registered prospectus is required in respect of the securities referred to in the investment statement, the latter must draw attention to the prospectus so that potential investors may examine the full documents.[13] The Act also places restrictions on advertisements (which include investment statements).[14]

[18] Part 2 of the Act imposes civil liability for non-compliance with the requirements of the Act. The court has power to award both compensation and pecuniary penalties. Criminal liability is provided for in ss 58, 59, 59A and 60. The section relied upon by the Crown in the present case is s 58 which, at the time of the events at issue, relevantly provided:

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9 Nine months from the last audited accounts to 31 March 2007.
10 Section 37A(1A)(c)(ii).
11 The Judge found that the Crown had not proved the registration and distribution of the extension certificate but nothing now turns on this. The Crown accepted that the amended prospectus was extended for 12 months to September 2008.
12 Section 38D.
13 Sections 38C–38E.
14 As defined by s 2A.

> **58 Criminal liability for misstatement in advertisement or registered prospectus**
>
> (1) Subject to subsection (2) of this section, where an advertisement that includes any untrue statement is distributed,—
>
> (a) The issuer of the securities referred to in the advertisement, if an individual; or
>
> (b) If the issuer of the securities is a body, every director thereof at the time the advertisement is distributed—
>
> commits an offence.
>
> (2) No person shall be convicted of an offence under subsection (1) of this section if the person proves either that the statement was immaterial or that he or she had reasonable grounds to believe, and did, up to the time of the distribution of the advertisement, believe that the statement was true.
>
> (3) Subject to subsection (4) of this section, where a registered prospectus that includes an untrue statement is distributed, every person who signed the prospectus, or on whose behalf the registered prospectus was signed for the purposes of section 41(b) of this Act, commits an offence.
>
> (4) No person shall be convicted of an offence under subsection (3) of this section if the person proves either that the statement was immaterial or that he or she had reasonable grounds to believe, and did, up to the time of the distribution of the prospectus, believe that the statement was true.
>
> …

[19] We have already referred to s 55 in relation to omissions but it is convenient to repeat it here:

> **55 Interpretation of provisions relating to advertisements, prospectuses, and registered prospectuses**
>
> For the purposes of this Act,—
>
> (a) A statement included in an advertisement or registered prospectus is deemed to be untrue if—
>
> (i) It is misleading in the form and context in which it is included; or
>
> (ii) It is misleading by reason of the omission of a particular which is material to the statement in the form and context in which it is included:
>
> …

The elements of the offences

[20] It was accepted that the relevant prospectus and the advertisements had been distributed. There was no dispute that the appellants had all signed the prospectus for the purposes of s 58(3) nor that they were all directors of Lombard for the purposes of s 58(1). The appellants also accepted that the charges they faced were offences of strict liability. The Crown was not required to prove any criminal intent on the part of the appellants.

[21] The only issues were whether the Crown had proved beyond reasonable doubt that the impugned offer documents included statements that were untrue and, if so, whether the appellants could establish the statutory defence on the balance of probabilities.

[22] In the present case, the prosecution relied on the omission of material to demonstrate that the amended prospectus was misleading. In such a case, the Crown must prove beyond reasonable doubt that the statements in the offer documents are misleading by reason of an omission that is material to the statements in the relevant offer document. The onus then shifts to the accused to establish on the balance of probabilities that the statements are immaterial or that he or she believed on reasonable grounds that the statements were true despite the omission.

[23] The appellants did not challenge the approach adopted by the Judge that a material omission is one that could well have made a difference to the decision whether to invest.[15] The notional investor for this purpose is one who was prudent but non-expert.[16]

[24] It is unnecessary to elaborate on the characteristics of the notional investor or the approach to interpreting a prospectus since neither of those topics nor the issue of materiality assumed any importance on appeal. Rather, the focus was on the truth of the statements in the amended prospectus and whether the appellants had reasonable

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15 See the helpful discussion by Heath J in *R v Moses* HC Auckland CRI-2009-004-1388, 8 July 2011 at [28]–[51] discussed at [24] of the verdicts judgment.

16 Picking up s 38D(a) of the Act.

grounds to believe that the statements were true despite the matters allegedly omitted.

Factual context

[25] Before addressing the specific grounds of appeal, we set out some factual context which is largely uncontroversial. We have relied primarily on contemporary documentary evidence as offering the most reliable evidence of the relevant events.

[26] Lombard had operated for some six years as a finance company. It was a wholly owned subsidiary of Lombard Group Ltd, a publicly listed company on the New Zealand Stock Exchange. Lombard was by far the major asset of its parent company. From time to time Lombard raised money from the public, borrowing both on a secured basis (with investors receiving debenture stock secured over Lombard's assets) and on an unsecured basis. Prospectuses were issued as required for this purpose and Lombard also publicly distributed investment statements promoting investment in its debenture stock and unsecured notes.

[27] At relevant times, Sir Douglas Graham was the chairman of Lombard's Board and Mr Reeves was the chief executive. The Hon Mr Jeffries and Mr Bryant were the other directors. Mr Reeves was the only executive director.

[28] The business model adopted by Lombard involved short-term borrowing from investors while lending generally over longer periods. Typically, Lombard's loans to developers were for terms shorter than the estimated period to complete the borrower's project. This was intended to enable Lombard to maintain pressure on the borrower. However, loans would normally be rolled over until completion provided satisfactory progress was being made.

[29] Lombard's principal sources of revenue were loan repayments, interest on loans, the fees charged for the loan facilities and investments made by members of the public. The repayment of the loans was dependent upon the completion of the borrower's development projects and the subsequent sale of properties. Interest on the loans was largely capitalised. New investments in Lombard and the roll-over of existing investments were very much dependent upon investor confidence.

[30] In March 2007 Mr Reeves reported to the Board that there was a general lack of confidence in the finance market as a whole although he was not aware of any negativity aimed at Lombard in particular. Despite that, Lombard was reported to have traded profitably in the year to 31 March 2007.

[31] By May 2007, concerns about Lombard's exposure to major borrowing groups led the company's auditors to recommend to the audit sub-committee of the Board that a separate sub-committee, including one or more independent directors, be established to monitor the larger loans. A principal focus of concern was a large development in Brooklyn, Wellington. This committee (which we will refer to as the large loans committee) was formed. It comprised Mr Bryant, Mr David Wallace (a director of Lombard's parent company) and Lombard executives.

[32] Although Mr Reeves was appointed to the large loans committee, the minutes of that committee show that he did not attend the meetings until November 2007. He explained in evidence that there were timing difficulties which generally prevented him from attending.

[33] In May 2006 two smaller finance companies had failed but in 2007 two major finance companies went into receivership: Bridgecorp Holdings Ltd on 2 July and Nathans Finance NZ Ltd on 20 August. Eight other finance companies collapsed between August and December 2007.[17] The minutes of the Board meeting on 25 July 2007 record that the demise of Bridgecorp had left the financial services market nervous but stated that it was encouraging to know that Lombard had such high cash reserves.

[34] Nevertheless, the collapse of these finance companies led to concerns being raised in the industry about the standing and liquidity of other companies in the market. The minutes of the Board meeting on 29 August 2007 record that the Board discussed at length a request by the Securities Commission for the directors to confirm Lombard's profitability. The minutes show that the Board concluded that the liquidity position of the company was strong with cash at $37 million. There had

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[17] Including Five Star Consumer Finance Ltd in August and Capital + Merchant Finance Ltd in late November.

also been an improvement in the security backing for the loan book. The company responded to the Securities Commission by noting that there had been no material adverse changes to Lombard's liquidity and asset quality analysis.

[35] Lombard's statutory trustee required under the Act was Perpetual Trust Ltd. Perpetual's concerns about Lombard's liquidity in mid-2007 led it to require Lombard to provide weekly reports on the company's liquidity and cash flow, in addition to other reporting requirements under the trust deed. Then, in August 2007, Perpetual asked Lombard to retain the accounting firm Ferrier Hodgson (later KordaMentha) to undertake an independent review of the company's loan portfolios and liquidity.

The Ferrier Hodgson report

[36] Ferrier Hodgson reported on 18 September 2007. The report was prepared by an experienced accountant, Mr Grant Graham. It commenced by stating:

> The New Zealand finance company sector has been under significant stress in recent times. Those with an exclusive or a predominance of debenture funding are under increasing pressure as reinvestment rates plummet from historical levels.

[37] Ferrier Hodgson reported that Lombard's cash profile reflected a "running down of the business". New lending had ceased, existing loans were being collected and debenture stock was being repaid. While this was intended to improve liquidity by increasing cash reserves, the report commented this was not a sustainable long-term business strategy. Ferrier Hodgson noted that this was not necessarily of concern to debenture stock holders.

[38] For the purposes of its report, Ferrier Hodgson adopted the company's own cash flow projections, noting that there was approximately $33 million of cash on hand at the date of the review and that this would "maintain a liquidity buffer over the next 12 months". An important proviso was that this was dependent on Lombard being able to collect the forecast loan repayments on the six major loans reviewed by Ferrier Hodgson. The cash flow projections depended upon all assumptions being achieved but, most critically, on loan repayments being received on the forecast dates. The report said that the assumptions made about repayments were not

unreasonable. Variances from expectations could be expected and the projections should be regularly revised as circumstances dictated.

[39] The Ferrier Hodgson report also provided an analysis of the cash flow expected to arise from new deposits and reinvestment rates in respect of maturing debenture stocks. As to the former, Lombard assumed that $250,000 per month would be received in new deposits between October 2007 and January 2008, which was said to be the monthly equivalent of the deposits received over the two weeks prior to the date of Ferrier Hodgson's review. This compared with historical trends which Lombard advised were approximately $1.5 million to $4 million per month. New deposits were expected to recover to a rate of approximately $500,000 per month by February but that assumed the market would stabilise and that Lombard would be able to differentiate itself as having better investment products than other finance companies.

[40] As to the repayment rates on maturing debenture stock, the report noted that, historically, there had been a reinvestment rate of between 60 and 70 per cent by value. Over the two weeks prior to Ferrier Hodgson's review, the rate of reinvestment had dropped to between 35 per cent and 40 per cent by value. Lombard's cash flow projections adopted a much more conservative approach, assuming that the rate of reinvestment would drop to five per cent during September before increasing each month to 60 percent in August 2008.

[41] The Crown did not dispute that Lombard's projections in relation to new investment and rates of redemption on existing investments were appropriately conservative.

[42] The significant matters to emerge from Ferrier Hodgson's report are:

- The company was in "running down" mode in order to reduce the loan book. No new loans had been made since March 2007 in order to maintain a liquidity buffer for the next 12 months although existing commitments were unaffected.

- New investment in the company had dropped dramatically compared with historical trends.

- The rates of reinvestment of maturing debenture stock had also dropped off substantially.

- The assumptions in Lombard's cash flow projections were critically dependent on loan repayments being received when projected.

- The cash buffer of $33 million then held by the company was regarded as important to its liquidity.

Events subsequent to the Ferrier Hodgson report

[43] When the Board met again on 26 September 2007, Mr Reeves reported concern about the future viability of finance companies which relied on funding from the issue of debenture stock. He is recorded as stating that he believed the lack of investor confidence following the failure of so many finance companies over the past 12 months was "serious and unlikely to be restored for some time". He suggested that the company should look to other means of augmenting revenue flows. Although alternative revenue streams were investigated, none of the alternatives considered was ultimately pursued.

[44] Despite these difficulties, Mr Reeves reported that the liquidity position at Lombard was still sound with about $24 million held in cash. Even if the company were wound down from that date onwards, it was estimated that, after recovery of all loans and repayments from all investors, there would be a surplus of at least $13 million. For the next 12 months or more, repayments of loans and cash held were thought to be sufficient to repay maturing deposits, even with the existing levels of reinvestment. Mr Reeves was reported as assuring the Board that the company would have no difficulty meeting the trustee's requirements.

[45] In late October 2007, Lombard asked Phillips Fox Solicitors (who had prepared the September prospectus) to review the prospectus in light of the changing financial circumstances. This was done and the draft later reviewed by Mr Foley, a lawyer at Minter Ellison Rudd Watts.

[46] Further cash flow projections were prepared for the Board meeting on 6 November 2007. The minutes record that the next six months would be tight especially if projected loan repayments did not eventuate. The success of the

projections relied on the company receiving a projected $30 million in loan repayments in November and December. During that month, an expected repayment of $10 million from the Brooklyn Rise development did not eventuate. Lombard's exposure to the Brooklyn Rise development was the largest of any of the company's six main borrowers. It is common ground that Brooklyn was poorly managed and Lombard was endeavouring to arrange a sale of the project to an Auckland developer who was expected to bring greater stability to the development. Ferrier Hodgson's report stated that the advances to Brooklyn totalled $45.523 million and represented 32 per cent of Lombard's total loan book.

[47] The minutes of the 6 November Board meeting also record that the Board discussed the likely impact on the company (and the resultant impact on deposits) if there were further finance company failures. The possibility of an alternative bank facility was regarded as most unlikely. According to the minutes, the Board advised Mr Reeves and Mr Alan Beddie (who was Lombard's chief financial officer until October 2007 and had previously been one of its directors) that they fully supported their liquidity management actions taken to that point.

[48] The large loans committee met on 15 November 2007. Sir Douglas Graham and Messrs Bryant and Reeves were present. There was a detailed discussion of the current position in respect of the principal developments and the projected dates for loan repayments. The minutes record that Lombard's cash reserves were then $10 million. This was said to be about $5 million lower than projected due to delayed repayments.

[49] No doubt as a result of this meeting, Sir Douglas Graham sent an email to Mr Reeves' private email address the same day expressing concerns about Lombard's liquidity. Relevantly, the email stated that Sir Douglas had no doubt that everyone:

> … is working hard to get the loans repaid or refinanced but the fact is that we are sailing very close to the wind now and the next two or three months will be critical. Some of our exposures are difficult and dependent on a number of positive events occurring. If they do not, or there are delays, we run the risk of running out of cash. I know that consideration is being given to obtain a line of credit from the bank but we both know how obstinate the banks can be and I do not think we can rely on that. A private placement of

> prefs may relieve the pressure but I have doubts it will succeed in the present climate with the exposures we have. I would not want to be a party to any capital raising which misrepresents the true position…

[50] The Board met again on 28 November 2007. Mr Beddie presented further cash flow forecasts. As at the date of the meeting, the minutes record that the company had $8 million in the bank which was expected to reduce to $6.17 million on 1 December 2007. Again, the Board discussed in detail the expected loan repayments and their timing in December and January. A "worst case" scenario in the projections showing no repayments of loans was also considered. It was noted that the company was "in a very vulnerable position if loan repayments were not received". Mr Reeves reported that several options were being pursued as to possible alternative funding arrangements. The Board agreed to defer discussion of any alternative arrangements until the December Board meeting. The chairman reiterated the Board's support for management in what was "a very challenging financial climate".

Events in December 2007

[51] During December, the amended prospectus earlier drafted by Phillips Fox was reviewed by Mr Foley. The Board met on 19 December. Further cash flow projections produced by Mr Beddie were discussed. The minutes record that, with cash on hand at the meeting date of $7.289 million, the projections indicated there were sufficient funds on hand to enable the company to meet its outgoings. The Board also considered actual loan repayments compared with those expected at the time of the last Board meeting. The minutes state that management provided reasons for the expectations not being met and updated the Board on the likelihood of current projections being met. The minutes then state:

> Although the projections showed that liquidity might be tight in March it was also understood that action to be considered and taken in the new year would improve the situation. Mr Beddie noted that a lot of work could be required to collect some of the loans and it would be a challenge to balance receipts and payments each month. Although it was hoped that the 2 major loans, Brooklyn and Bayswater and totalling approximately $50m, might settle early in 2008, it was obvious that if they didn't then they would be the major components of the book which was expected to reduce to $110m - 115m at year end, and $90m at 30 June.

[52] The Board resolved to approve the amended prospectus and the related certificate. The meeting closed with the chairman reiterating the Board's support for management, noting again the very challenging financial climate.

Events post-Christmas 2007

[53] The focus of the case at trial was on events up to 24 December 2007 when the amended prospectus was issued. We do not intend to dwell on events after Christmas 2007 except to record that Lombard's financial position deteriorated further and, on 2 April 2008, Lombard announced it was suspending repayments to investors. The appointment of receivers followed on 10 April 2008.

The witnesses

[54] The Judge received a large volume of evidence both documentary and oral. The Crown's principal evidence was given by Ms Michelle Peden who was employed by the Securities Commission as an investigating accountant. The Crown also called as an expert Mr Charles Cable, a corporate finance partner with the accounting firm Deloitte. Mr Cable had been asked to critique a report prepared by Ms Peden and to offer an opinion on certain issues relating to the adequacy and accuracy of the amended prospectus. The Crown also relied on evidence of Mr John Fisk, one of two partners of PricewaterhouseCoopers who were appointed as Lombard's receivers. Mr Fisk gave evidence about the financial state of the company after his appointment and an overview of the realisation of securities held for the major advances. Mr Andrew Dinsdale and Mr Ross Buckley were called to give evidence in their role as partners of Lombard's auditors, KPMG. Another important witness for the Crown was Mr Graham, who had been responsible for the Ferrier Hodgson report of September 2007 and for part of the work associated with a later report in April 2008. Ms Stephanie McGreevy gave evidence as the executive with Perpetual responsible for monitoring Lombard's compliance with the obligations under the trust deed. Evidence was also received from some of Lombard's investors.

[55] For the defence, each of the appellants gave evidence and Sir Douglas Graham called an additional nine witnesses. These included three Lombard

employees, one of whom was Mr Beddie. The former company secretary, Mr Peter Morpeth, gave evidence along with Mr Foley. Mr Wallace also gave evidence as chair of Lombard's parent company and as chair of Lombard's large loans committee. Other evidence was called from a solicitor retained by Mr Tim Manning, whose company had taken over the Brooklyn Rise development in November 2007. Mr David Newman, an experienced company director, gave evidence about the skills required of company directors and the situation facing company directors in late 2007 and early 2008. The expert witness for the defence was Mr David Appleby, a senior chartered accountant with experience as a company director. He gave evidence relating to the financial performance of Lombard, the standard of decision-making by the Board and the allegedly untrue statements in the offer document.

The relevant parts of the amended prospectus

[56] In relation to the issue of liquidity under the first particular of count one, the indictment stated:

> The presentation of 'liquidity risk' omitted material particulars namely actual and significant adverse liquidity issues including; the deterioration in the cash position from the balance of 30 September 2007, the failure to achieve forecast (internal and Ferrier Hodgson) cash receipts and loan repayments.

[57] Specific parts of the amended prospectus were then identified but the Crown stated that it relied on the entire statement under the heading "Liquidity Risk" at pages 12 and 13 of the amended prospectus. We set this out in full since, although it is a lengthy passage, the overall impression is important:

> **Liquidity Risk**
>
> Liquidity risk is a risk of Lombard Finance not having enough cash liquidity to meet its obligations as they fall due. In the event that Lombard Finance failed to manage its liquidity, due to mismanagement of its own borrowings (deposits from investors) or matured loans failed to repay on time and should such loss of liquidity be of a magnitude to cause Lombard Finance to become insolvent, there could be insufficient funds to repay investors.
>
> Lombard Finance in its normal course of business allows clients where appropriate (for example for the building phase of a development loan) the option of capitalising interest and fees. The amount of interest and fees capitalised in the accounting period to 31 March 2007 totals $15.95 million ($7.02 million in the 6 month period to 30 September 2007). This non cash

income is recorded in the profit for the year, however this deferral of cashflow until the maturity of the loan is offset by receiving the interest and fees in cash for the maturing loans during the year. To understand the cashflows it is important to look at the cashflow statements in the accounts attached to this Prospectus. This statement shows that Lombard Finance's investing and operating activities produced a cash surplus for the year of $14.603 million (after adjusting for the $2.632 million decrease in loans and advances) ($1.453 million in the 6 month period to 30 September 2007 after adjusting for the $18.097 million decrease in loans and advances). The cash surplus for the 2006 year after adjusting for the change in loans and advances was $10.787 million ($1.453 million in the 6 month period to 30 September 2007).

Lombard Finance manages its liquidity by regularly updating its projections of:

- The maturity dates of amounts owed to investors
- The proportion of investors that will redeem, as opposed to reinvest, their investments
- Loan repayments received from borrowers (often from the expected sales of completed developments)
- Further advances made to borrowers, including further advances made as part of funding of developments. At the date of this prospectus Lombard Finance does not have significant commitments to fund ongoing developments (funds committed for ongoing development will vary from time to time).

Reports are provided to the Board weekly and are available to the Credit Committee whenever it assesses a loan proposal or any other dealing with a borrower.

In common with other companies in the finance sector, Lombard Finance is currently experiencing a reduced level of reinvestment by borrowers that [sic] applied 12 months ago. Cash flow projections are completed on a conservative basis (meaning that a lower level of reinvestment is used for this purpose than is currently being experienced and allowances are made for delays in borrowers repaying their loans which recognise that in current circumstances the sales of properties are being delayed).

If market confidence in the finance sector continues to decrease (particularly if there are further failures of finance companies) new investment and renewals may decrease below the levels that Lombard Finance is currently achieving, which may impact on liquidity. The Board remains confident that, based on a range of conservative scenarios, Lombard Finance will have the required cash resources to fund all repayments to investors when due and that are not reinvested. A period of constrained liquidity will also impact on the company's capacity to lend and is likely to negatively impact on Lombard Finance's future growth and profitability. A current impact of this is the reduction in current loans made by the Company from $167.6 million on 30 September 2006 to $144.3 million on 30 September 2007.

There is a risk that a further loss of confidence in the finance sector could result in investors materially reducing their level of reinvestment below that assessed by Lombard Finance. If that was extreme, Lombard Finance would not be able to fund its repayment obligations

> **unless other funding was available or asset realisations/borrower repayments were accelerated.**
>
> **Capitalising Loans**
>
> The majority of Lombard Finances' loans involve the capitalisation of interest and fees with payments of interest, fees and principal not due until the end of the loan term. If this is not managed it could lead to the borrower's equity in the security for the loan being diminished, leading to an increased risk of recovery on the loan. Lombard Finance manages this risk by assessing the loan to security value ratio before advancing the loan by taking into account the capitalised position at the end of the loan term.
>
> (Emphasis in original.)

The Judge's findings

Liquidity

[58] The Judge was satisfied beyond reasonable doubt that the amended prospectus was misleading in relation to Lombard's liquidity position. He found there were three factors which, when combined, supported this conclusion:

- the omission of statements describing the lack of reliable forecasts about the timing of loan repayments on which Lombard's liquidity depended;
- the omission of any acknowledgement about the reduction in the cash on hand; and
- the omission of any reference to directors' concerns on that topic.

[59] The Judge also concluded that the amended prospectus did not bring home to potential investors that the identified risks were imminent. The Judge expressed his view on this issue in these terms:[18]

> Reflecting on all the passages in the amended prospectus that bear on the issue of liquidity, I find that they do not reflect a concern at the time it was issued that there was an existing risk that [Lombard] might run out of money in the forthcoming months. I accept that the conditional language in which certain risks relevant to liquidity were described would reasonably have conveyed to readers of the amended prospectus that the directors were not concerned that the adverse circumstances described existed at the time, or were imminent.

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[18] At [92].

[60] Addressing the cash position, the Judge found that, from around the middle of 2007, the directors had foreshadowed a period of tighter liquidity and had decided to bolster cash reserves.[19] That had resulted in unusually high cash reserves, reaching a maximum of some $39.6 million in August 2007, dipping to $7.2 million by December 2007.

[61] The Judge was not satisfied that the amended prospectus was misleading in not stating the specific cash balance available to the company on the date it was issued. That was because there were significant fluctuations in the cash balance from day to day and because there were other factors impacting on the relative adequacy of a cash balance. However, as the Judge put it:[20]

> … that does not relegate the trend in the company's cash position to immateriality, given its importance as a component of the liquidity position which was of paramount importance in December 2007. The directors knew, and were seriously concerned about, the deteriorating cash position. In the end, the prospect of a cash crisis was just that: the less cash [Lombard] had, the more vulnerable it was to not being able to meet its obligations. The trend in recent months showed the extent of cash dropping consistently, to the extent that the chairman perceived the company as "sailing very close to the wind". It was inarguably material to investors that the cash available to the company had reduced markedly in recent months, and was a cause of concern to the directors.

[62] As to the discrepancy between Lombard's cash projections and the actual performance of the company during the last quarter of 2007, the Judge found that:[21]

> By the time of the preparation of Board papers for the 19 December 2007 Board meeting (using figures as at 12 December 2007), the actual extent of cash at the end of November was reported at $9.47 million (compared with projections used by Ferrier Hodgson, and since then, of $28.3 million, $16.3 million, and $23.6 million). The projection for December 2007 was $8.8 million, (compared with equivalent projections of $30 million, $15.7 million and $22.9 million).

[63] The Judge found that the main cause of the cash position being worse than projected was delays in loan repayments. Although management had been monitoring the prospects of the payments on the company's major loans closely and reporting regularly to the Board, the forecasts about the timing of loan repayments

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[19] At [104].
[20] At [118].
[21] At [104] bullet point seven.

erred substantially. Based on a schedule prepared by Ms Peden, the Judge found that Lombard had received 13.9 per cent of the repayments projected in the previous month for September 2007; 36.4 per cent for October 2007; 69.7 per cent for November 2007 and 55 per cent for December 2007.[22] The Judge found that, cumulatively, the repayments over those four months were 46 per cent of the amounts projected. Ms Peden's schedule was the subject of sustained criticism at trial and also before us. We return to it later in this judgment.[23]

[64] The Judge went on to find that the appellants were relying on assurances from the lending managers responsible for the various loans to the effect that the delays in loan repayments were capable of being explained and that the borrowers would still be able to perform despite payments being made later than previously projected. The appellants assessed the loan managers to be competent but the Judge found they did not attempt to independently check the reasonableness of the managers' assessments.

[65] The Judge was satisfied that potential investors would assess the risk of investing in Lombard's debenture stock differently in material respects had they been given the essence of the matters he found ought to have been included in the amended prospectus on the issue of Lombard's liquidity.[24] He considered that the appellants' continued reliance on the projections for recovery of loan repayments notwithstanding a pattern of errors substantially overstating those repayments, would have been material information. The Judge said:[25]

> … Potential investors would be likely to question the prudence of the directors' judgement in continuing to rely on the loan managers in this regard, or might take from such information that conditions in the market were so unpredictable that projections could not reliably be made. In either event, such prospects render the omission of information on the topic from the amended prospectus a material one, in respect of a matter that is adverse to the financial standing of [Lombard].

[66] In reaching his conclusions, the Judge considered and rejected a number of points made by the appellants or on their behalf. He did not accept that the period

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22 We note that the 55 per cent figure for December was not available until after the Board approved the prospectus.
23 At [109]–[115] and [154]–[160].
24 At [105].
25 At [106].

over which the overstating of projected loan recoveries had continued was insufficient to constitute a pattern. And, despite the availability of individual explanations for delay in the loan repayments for particular loans, the overestimations were considered by the Judge to be substantial to an extent that was important to the survival of the company. By the time the amended prospectus was issued, the Judge found there was a discernible pattern of overstatement in projected loan recoveries that constituted information that would be important to potential investors.[26]

[67] The Judge also rejected a defence proposition to the effect that it was a matter for the directors to make a commercial judgement about the company's prospectus and investors could rely on the directors to exercise that judgement. It had been contended that the relative reliability of the loan repayment projections was a matter for the directors and did not need to be included in the amended prospectus. On that point, the Judge said:[27]

> However, such an approach misunderstands the rationale for the disclosure regime. It is intended that investors be in a position to make decisions for themselves by being adequately informed on material matters, rather than making an investment decision in reliance on an assessment of the quality of judgement of those who would become custodians of their investments.

[68] The Judge did not accept Mr Appleby's opinion that the extent of variance between projections relied upon by the Board from month to month and the actual outcomes was not a matter of interest to the investors. In circumstances of tightening liquidity, the Judge considered investors were entitled to know the quality of Lombard's performance in managing its major loan exposures. The accuracy of the company's projections as to the timing of repayments was one useful barometer of that level of success.[28]

[69] The Judge went on to note that one of the cash projections considered by the appellants at the Board meeting on 19 December 2007 showed that, if no further loan repayments were received at all, Lombard would run out of money on 16 January 2008. The Judge accepted this was a pessimistic projection produced as a worst case

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26 At [107].
27 At [109].
28 At [110].

scenario. However, if the appellants had recognised the pattern of overestimation of loan recoveries and adopted a projection of 50 per cent of the predictions by the loan managers, then Lombard would have briefly run out of money shortly before 18 January 2008. It would have had sufficient cash thereafter to survive until the end of February but would have been unable to meet its commitments from then on. The Judge then added:[29]

> In fact, [Lombard] had sufficient cash to meet its obligations for another month after that. However, eliminating hindsight and reflecting on a reasonable prospective view as at 24 December 2007, some such projection applying the company's recent experience would have been prudent. Any acknowledgement of the poor quality of projections about loan repayments would have raised doubts about the confidence expressed in the adequacy of cash resources.

[70] The Judge considered that the amended prospectus might have read along the following lines:[30]

> Since mid 2007 [Lombard] has sought to build and maintain cash reserves to guard against the reduced investment and reinvestment rates likely to be caused by the loss of investor confidence in the finance company market. The company's cash reserves reached a high of approximately $40 million in August 2007, and although the amounts fluctuate, the downward trend during December 2007 has been to around 22-18 per cent of that high point. A substantial majority of the cash reserves have been applied to repay maturing investments.
>
> The adequacy of [Lombard's] cash resources is a source of concern to the directors. The company's ability to meet its obligations to investors in the coming months depends upon receipt of loan repayments as forecast. The directors are dependent on the respective loan managers for projections as to the timing and amount of loan repayments. Since September 2007 there has been a substantial extent of over-estimation in the projected loan repayments, month by month. However, the directors continue to have confidence in the competence of the loan managers and provided there is a material improvement in the accuracy of their projections, [Lombard] will be able to continue meeting its obligations as they fall due.

[71] The Judge recognised that, in a commercial sense, there might be little point in issuing a prospectus that was expressed in such cautionary terms. However, he considered this could not influence the analysis of what was required to provide adequate and accurate disclosure. This too is a point challenged by the appellants and we will return to it.

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29 At [115].
30 At [121].

Impairment of major loans

[72] As at the date of the Ferrier Hodgson report in September 2007, the amounts outstanding on the six major loans reviewed were (in round figures):

Brooklyn Rise	$45.5 million
Bayswater Apartments	$12.8 million
Der Rohe Holdings	$14.0 million
Blue Chip companies	$10.0 million
Odonn[31]	$2.0 million
Hawke Bay Property Holdings	$11.6 million

[73] These loans totalled nearly $96 million which, as earlier noted, represented about 68 per cent of Lombard's property-related loans of approximately $136.8 million.

[74] The Judge undertook an extensive analysis of the Crown's allegation in the second particular of count one, that the amended prospectus was untrue because it omitted material relating to adverse impairment and recoverability issues for the loans Lombard had made to its major borrower groups. We do not propose to set out the Judge's detailed findings on this issue since he ultimately decided that the Crown had not made out this allegation beyond reasonable doubt except in relation to the Bayswater loan which had reached a level of $15.7 million in early December 2007. The Judge found there were numerous "red flags" suggesting that the advance to Bayswater was not fully recoverable. Nevertheless, he accepted that the failure to disclose that this loan was impaired was not shown to be material in relation to Lombard's overall financial position.

[75] The appellants rely on the Judge's finding on the impairment issue to support their argument that the Judge's verdict on the liquidity issue was unreasonable or not supported having regard to the evidence. While we accept that the Judge's finding on the impairment issue is relevant to liquidity, we do not regard it as a determinative factor. A loan may ultimately be recoverable in full and therefore not impaired in the sense relied upon by the Crown. However, Lombard's survival depended critically

[31] A company associated with Mr Mark Bryers.

on cash flow. The concern for liquidity purposes was with the timing of repayments rather than whether the loans might ultimately be recovered by the completion and sale of a development or by other means such as re-financing.

[76] This was well understood by the appellants and Lombard's management throughout the second half of 2007 and particularly in the last quarter. While the Judge was not satisfied there was a sufficient pattern of delayed sales to require recognition of impairment,[32] there can be no question that there were significant delays by borrowers in meeting the milestones for loan repayments and that these were of real concern to the appellants.

Adherence to lending and credit policies

[77] The appellants also relied on the Judge's finding in their favour on the third particular of count one relating to adherence to lending and credit policies. It is not necessary to set out the Judge's detailed findings in this respect. We accept that his finding is relevant to the overall picture but we do not regard the finding as determinative.

First ground of appeal – misdirection on the approach to omissions under s 55 of the Act

Appellants' submissions

[78] On behalf of the appellants, Mr Farmer QC submitted that the Judge had misdirected himself by adopting the approach that s 58(3) of the Act was concerned not only with the accuracy or truthfulness of the material in the amended prospectus but was also concerned with the adequacy of the material. Counsel pointed to the Judge's observation that:[33]

> … the law has created criminal liability for what may be no more than a material misjudgement about the accuracy and adequacy of the description of the state of financial health of the company …

[79] Counsel also referred to the observation by the Judge we have already referred to at [67] above that the Act intends that investors be in a position to make

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[32] At [178].

[33] At [10].

decisions for themselves by being adequately informed on material matters rather than making investment decisions relying on the quality of judgement of the directors.

[80] It was submitted that the Judge had erred by failing to recognise the separate purpose of the disclosure regime in Part 2 of the Act and the purpose of the criminal sanctions in s 58. In short, counsel submitted that s 58 was not concerned with the adequacy of disclosure. Rather, it was concerned with the truthfulness or accuracy of the statements made in the prospectus. While recognising that s 55 provided that a statement in a prospectus could be deemed to be untrue if it were misleading by omission, counsel emphasised that any such omission must be "material to the statement in the form and context in which it is included".[34] That meant criminal liability did not attach to any general failure by the appellants to provide adequate information. Rather, criminal liability for omitted material attached only if it resulted in a statement in the prospectus being misleading and therefore untrue in the statutory sense. Counsel referred to Venning J's observation in *R v Petricevic* that:[35]

> … It is not an offence to omit something from the prospectus unless that omission makes a statement in the prospectus untrue.

[81] Counsel referred us to the extensive provisions in the Act and in the Securities Regulations specifying the contents required for a prospectus and other offer documents.[36]

Discussion and decision

[82] We do not accept the submission that the Judge misdirected himself on this point. As this Court said in *R v Steigrad*, the purpose of the Act is to protect the investing public through timely disclosure of material information.[37] In that respect,

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34 Section 55(a)(ii).
35 *R v Petricevic* [2012] NZHC 665, [2012] NZCCLR 7 at [212].
36 Particularly ss 39–41 of the Act, the matters that were required by Part 1 of the Securities Regulations 1983 to be included in a prospectus and the provisions of Part 1A of the Regulations as to the contents of investment statements. See also Part 2 of the Regulations that apply to the content of advertisements
37 *R v Steigrad* [2011] NZCA 304, [2011] NZCCLR 24 at [74].

the Court adopted the following statement by Richardson J in the earlier decision of this Court in *Re AIC Merchant Finances Ltd* that:[38]

> … The pattern of the Securities Act and the sanctions it imposes make it plain that the broad statutory goal is to facilitate the raising of capital by securing the timely disclosure of relevant information to prospective subscribers for securities. In that way the Act is aimed at the protection of investors. That aim is achieved by regulating the conduct of issuers of securities and by providing sanctions for infringement by those issuers and their officers …

[83] In *Steigrad*, this Court accepted that this interpretation was: [39]

> … consistent with a broader view of the context of financial markets that recognises that all offers of securities to the public (including all distributions of prospectuses or advertisements) involve information asymmetries between those soliciting and those investing funds. Money is solicited from an investing public that is highly dependent upon the truth of disclosure at the time of investment.

[84] This Court went on to say that the risk of untrue statements is a direct challenge to the integrity of this regime and that those seeking funds are in the best position to guard against that risk.[40]

[85] The Act and the Regulations make it abundantly clear that the statutory intention is to prohibit false or misleading material in a prospectus. In this respect we have already mentioned s 34(1)(b) of the Act which prohibits the distribution of a registered prospectus which is false or misleading in any material particular. That may arise from either a failure to refer to adverse circumstances or to give proper emphasis to any such adverse circumstances. The Securities Regulations in force at the time also required additional information to be provided in a prospectus if a statement required in the prospectus would be misleading without that additional information.[41]

[86] Criminal liability under s 58 of the Act is properly viewed as supporting the disclosure regime by the imposition of criminal sanctions. The obligation not to include false or misleading statements in a prospectus or other offer document

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38 *Re AIC Merchant Finance Ltd* [1990] 2 NZLR 385 (CA) at 391–392.
39 At [75].
40 At [76].
41 Securities Regulations 1983, reg 5(1); see also reg 8 which prohibits an advertisement containing information likely to deceive, mislead or confuse.

extends by s 55 to the omission of material information that would render statements included in the prospectus or other offer documents to be misleading. That is consistent with the general purpose of the disclosure regime itself.

[87] We accept the submission made by Mr Carruthers QC on behalf of the Crown that, when the Judge referred to both the "accuracy and adequacy" of the information contained in the prospectus, he was doing no more than referring to the need to ensure that statements made in the prospectus were not false or misleading by the omission of material matters. In that sense, statements made in a prospectus could be inadequate as well as inaccurate.

[88] We are satisfied the Judge well understood that s 58 did not impose criminal sanctions on the basis of a general obligation to disclose material information unrelated to the accuracy of statements contained in the prospectus. That is clear from the whole tenor of his judgment and the identification of the three specific respects in which he found the statements in the prospectus were untrue through omission. In each case, the omissions related to statements already contained in the prospectus which the Judge found were misleading (and therefore untrue) in the absence of the omitted material.

[89] For example, although the amended prospectus referred to the risk of delayed loan repayments, it did not refer to the pattern of marked discrepancies between the company's projections and the actual receipt of funds. And, in conveying an impression of the directors' confidence about the ability of the company to repay investments when due, the amended prospectus omitted to mention the serious reduction in cash on hand and the directors' concerns about that. While identifying potential risks, the prospectus did not bring home the imminence of them.

Second ground of appeal – the Judge's conclusion that the statements in the prospectus were untrue was unreasonable or could not be supported having regard to the evidence

Approach on appeal

[90] The appellants mounted a substantial attack on the factual findings of the Judge, relying on s 385(1)(a) of the Crimes Act 1961. Under that provision, this

Court must allow the appeal if it is of the opinion that the verdict should be set aside on the ground that it is unreasonable or cannot be supported having regard to the evidence.

[91] It is important to recognise at the outset that the approach of this Court in criminal cases is materially different from the approach on a general appeal. In *Owen v R*, the Supreme Court confirmed that a verdict will be unreasonable in terms of the first limb of s 385(1)(a) if, having regard to all the evidence, the jury could not reasonably have been satisfied to the required standard that the accused was guilty.[42] It was recognised that there was no practical significance in the difference between an unreasonable verdict and one that could not be supported having regard to the evidence. A verdict that was unsupported by the evidence must necessarily be unreasonable. And an unreasonable verdict was one that had insufficient evidence to support it.[43]

[92] The Supreme Court in *Owen* also endorsed the following aspects of this Court's decision in *R v Munro*:[44]

> (a) The appellate court is performing a review function, not one of substituting its own view of the evidence.
>
> (b) Appellate review of the evidence must give appropriate weight to such advantages as the jury may have had over the appellate court. Assessment of the honesty and reliability of the witnesses is a classic example.
>
> (c) The weight to be given to individual pieces of evidence is essentially a jury function.
>
> (d) Reasonable minds may disagree on matters of fact.
>
> (e) Under our judicial system the body charged with finding the facts is the jury. Appellate courts should not lightly interfere in this area.
>
> (f) An appellant who invokes s 385(1)(a) must recognise that the appellate court is not conducting a retrial on the written record. The appellant must articulate clearly and precisely in what respect or respects the verdict is said to be unreasonable and why, after making proper allowance for the points made above, the verdict should nevertheless be set aside.

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42 *Owen v R* [2007] NZSC 102, [2008] 2 NZLR 37 at [5] of the judgment of Tipping J speaking for the Court.

43 At [5] and [12].

44 *R v Munro* [2007] NZCA 510, [2008] 2 NZLR 87 endorsed at [13].

[93] It has long been established that the verdict of a judge sitting alone is to be treated for appeal purposes as the equivalent of the verdict of a jury and may be challenged on the grounds that it is unreasonable or cannot be supported having regard to the evidence. Section 385(1)(a) applies equally to a judge alone trial. This Court on appeal is not authorised to retry the case on the facts.[45]

[94] In *R v Slavich* this Court considered whether an appellant who has been tried by judge alone is in a better position on appeal than he or she would have been had the facts been found by a jury.[46] The Court noted that this was an issue the permanent court might need to consider at some stage.[47] Without giving a definitive answer, the Court said that, probably, an appellant gets the advantage of a "fuller" appeal if his or her trial has been before a judge alone who has delivered full reasons, citing the decision of the Supreme Court of Canada in *R v Biniaris*.[48]

[95] However, the statutory ground of appeal under s 385(1)(a) remains the same irrespective of whether the appellant is tried by a judge sitting alone or by judge and jury. The court on appeal does not retry the appellants on the facts. The test to be applied is as stated in *Owen*.

[96] Mr Farmer did not dispute these principles and accepted the proposition put to him by the Court that if the verdict of the Judge was reasonably open on the evidence then the appellants could not succeed on the s 385(1)(a) ground of appeal.

The essence of the Crown's case

[97] The essence of the Crown's case on the liquidity issue was that the amended prospectus did not accurately portray the seriousness of Lombard's position in that respect. In particular, the following statement was said to be at odds with the reality of the company's liquidity position:

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45 *R v Connell* [1985] 2 NZLR 233 (CA) at 237; *R v Eide* (2004) 21 CRNZ 212 (CA) at 216; and *Wenzel v R* [2010] NZCA 501 at [39].

46 *R v Slavich* [2009] NZCA 188.

47 At [33].

48 *R v Biniaris* 2000 SCC 15, [2000] 1 SCR 381 at [37].

> The Board remains confident that, based on a range of conservative scenarios, Lombard Finance will have the required cash resources to fund all repayments to investors when due and that are not reinvested.

[98] On the Crown's case, the liquidity and cash position of the company had significantly and adversely deteriorated over the period September to December 2007 and the failure to disclose this in the offer documents was a material omission that rendered the statements misleading and therefore untrue.

[99] Although the amended prospectus referred to risks associated with an investment in Lombard at the end of 2007, on the Crown's case, it did not sufficiently convey the imminence of those risks or the real concerns the directors clearly entertained in the difficult economic climate experienced during that year.

[100] The company had begun to "re-trench" (as Mr Graham put it in his evidence) as early as March 2007. This was in an effort to reduce the loan book and thereby improve liquidity. However, concerns were heightened after the collapse of Bridgecorp and Nathans Finance in July/August. These adverse market events shook confidence in the finance company sector and led to Perpetual, as statutory trustee, requiring Lombard to obtain an independent report on the company's liquidity. It also led to a significant tightening of Lombard's reporting obligations to Perpetual.

[101] More specifically, the Crown case was that the amended prospectus did not reveal the reduction in Lombard's cash reserves which impacted on its ability to repay investors on maturity, nor the fact that there was a significant disparity between the forecast loan repayments and their actual repayments. In that respect, the Crown relied primarily on the evidence of Mr Fisk, Mr Cable and Ms Peden.

Mr Fisk's evidence

[102] Mr Fisk's evidence was that by 30 November 2007, the company's cash reserves had reduced to $9.2 million, some $19 million below the $28.3 million Lombard had projected in September when the Ferrier Hodgson report was prepared. The cash balance at 19 December was $7.2 million and $8.2 million at 24 December. By the time of the receivership on 10 April 2008 Lombard's cash position had reduced to $0.5 million from $36.5 million as at 1 September 2007.

[103] Of course, the cash projections were subject to frequent change as would be expected from a finance company of this type. Indeed, Mr Beddie was updating the cash projections on a daily basis during the last quarter of 2007. For the purposes of the Board meeting on 19 December, Mr Beddie produced three cash flow projections. Two were on a daily basis from 1 December 2007 to the end of February 2008. The third was on a monthly basis from December 2007 to November 2008.

[104] The first daily cash flow (the "worst case" forecast) assumed that no more funds would be received after 19 December. This was said to show that the company could meet payments due only until 4 January 2008 and that the company would run out of funds altogether by 16 January. The second daily cash flow assumed payments would be received as projected and that the company would have a cash balance at 24 December of $18.2 million. This was based on an assumption that loan repayments of $14 million would be received on 20 December. This cash flow also showed cash balances of between $10 million and $17 million over January and February 2008.[49]

Mr Cable's evidence

[105] However, according to Mr Cable's evidence, even the more favourable daily projection was substantially higher than the amounts actually received. A total of $19.2 million was forecast to be received during December up to the 20th of that month. $5.3 million was actually received between 1 and 18 December (prior to the 19 December Board meeting) with the balance of $14 million due on 19/20 December. In fact only $5.2 million was received between 19 and 21 December (after the Board meeting but before the amended prospectus was issued). No more was received before the end of December.

[106] The upshot was that only $10.6 million[50] of the $19.2 million in cash receipts forecast to be received between 1 and 20 December was actually received. This must have been known at least to management and to Mr Reeves as chief executive before the amended prospectus was registered. Mr Cable said that, in consequence,

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49 The monthly cash flow showed moderate cash balances from December 2007 for 12 months.
50 Rounded up slightly.

Lombard's cash balance at 24 December was only about $8 million rather than the projected figure of approximately $17 million. The cash balance of $8 million also contrasted with the figure of $24 million shown in Lombard's accounts as at 30 September 2007. The $8 million was insufficient, Mr Cable said, to cover the net debenture maturities which were projected to require $6 million per month throughout 2008. Mr Cable also said that, for at least four months prior to 24 December, the actual loan repayments had been materially lower than those forecast.

[107] Mr Cable's opinion was that the amended prospectus was misleading in these respects:

- By omitting to disclose the matters in [106] above.
- By omitting to state that, on the worst case forecast, Lombard would have exhausted its cash resources by 16 January 2008 if no loan repayments flowed as forecast.
- By stating that the Board remained confident that it had the required cash resources to fund all the payments to investors when due.
- By stating the risk to investors on a conditional basis ("in the event that … matured loans failed to repay on time … there could be insufficient funds to repay investors"). Mr Cable's opinion was that, at best, this was a statement of the obvious. He saw the statement as implying an absence of the actual liquidity issues that existed at the date of registration of the amended prospectus on 24 December.
- By stating in the directors' certificate that the amended prospectus was not false or misleading in a material particular by failing to refer, or give proper emphasis, to adverse circumstances.

[108] In his view, all these matters were material to potential investors.

Ms Peden's schedule

[109] During the cross-examination of Sir Douglas Graham, a schedule of figures prepared by Ms Peden was put to him. It had not previously been produced in evidence. There was initial concern by defence counsel (not Mr Farmer) about the production of this schedule which was an analysis by Ms Peden of data drawn from

material already in evidence. The Crown offered to recall Ms Peden if the defence considered it necessary to do so but that offer was not taken up.

[110] Six days later, the schedule issue arose again during the Crown's cross-examination of Mr Beddie. The Judge ruled that cross-examination on this topic should not continue at that time but left open the possibility of Ms Peden and Mr Beddie being recalled if required. Defence counsel advised that any application to recall Ms Peden would be resisted.

[111] In the event, there was no application to recall either Ms Peden or Mr Beddie but the defence called evidence some eight days after Mr Beddie's evidence from Mr Gray, an accountant formerly employed by Lombard. His evidence was critical in certain respects of the conclusions reached by Ms Peden in her schedule.

[112] Mr Farmer initially submitted to us that there had been a breach of natural justice or a procedural flaw in relation to the production of Ms Peden's schedule. However, ultimately he did not press that objection. He was right not to do so since the defence at trial declined to take up the Crown's offers to recall Ms Peden and, in any event, the defence were not disadvantaged by the course of events since there was an opportunity to comment on the schedule. The schedule was placed in the Crown's bundle of documents without objection. No risk of miscarriage arises.

[113] The general thrust of Ms Peden's schedule was to identify the wide discrepancy between Lombard's forecast loan repayments and the actual amounts repaid, particularly over the period September to December 2007. It was on the basis of Ms Peden's schedule that the Judge found that, cumulatively, the repayments over this period were only 46 per cent of the amounts projected.[51]

[114] The Crown naturally relied on Ms Peden's evidence to support its case. The schedule showed forecast loan repayments and drawdowns at various stages over the period August to December 2007 and compared those forecasts with actual repayments and drawdowns over the period. As a percentage of those forecasts, the monthly average repayments were:

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51 See [63] above.

September	13.9 per cent
October	36.4 per cent
November	69.7 per cent
December	55.0 per cent

[115] The cumulative average discrepancy in these figures was said to be 46 per cent. These figures were criticised at trial for accuracy and their relevance disputed as we later discuss.[52] But the Crown's case was that the significant point to emerge was the trend and scale of the inaccuracies. By the end of November 2007, only $22.4 million had been actually received compared with the company's forecast for loan repayments of $49 million at the time of the Ferrier Hodgson report in September. This discrepancy was reflected in the continuing deterioration of the company's cash reserves of approximately $33 million at the date of Ferrier Hodgson's report down to $7.2 million at the date of the 19 December Board meeting.

Other matters relied upon by the Crown

[116] In addition, the Crown relied on the importance Lombard attached to its cash reserves to support its ability to meet its repayment obligations to investors when required; the directors' awareness and concern about the tightening financial climate; their recognition, as reflected in the minutes of the meetings, that the company was vulnerable; Sir Douglas Graham's observation in November 2007 that "we are sailing very close to the wind now"; and the continuing willingness of the directors to accept the assurances of management despite the evidence available to them of the company's deteriorating cash position and the obvious discrepancies between the cash flow projections and repayments actually received.

The defence evidence

[117] We have set out at [55] above the witnesses for the defence. We outline first the evidence given by Sir Douglas Graham as chairman of directors since his evidence reflects in general terms the evidence given by the other appellants. Sir Douglas, in common with the other appellants, had extensive experience as a

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52 At [155]–[160].

company director. He saw his role as chairman as being to ensure the Board worked diligently and professionally with a clear demarcation between the roles of directors and those of management. Systems were put in place to ensure that directors received regular and accurate information from management. The Board did not approve loans made by the company but relied on a management team which the directors regarded as competent. Sir Douglas saw the Board's role as being to set policy with which management was to comply and to monitor management's oversight of the loan book.

[118] At the time of Lombard's incorporation in 2002, the company inherited a loyal following of investors from Lombard's predecessor.[53] Sir Douglas viewed his obligations to the depositors as being akin to that of a trustee to a beneficiary. During the early years after incorporation, the company performed well and had traded profitably in the year to 31 March 2007. However, given tightening economic conditions, the directors decided in early 2007 that it was prudent to begin to accumulate cash. The company had, from inception, a rule of thumb to retain in cash some 10 per cent of deposits.

[119] Despite the reduction in cash reserves from $39 million in August 2007 to $9.5 million by December, this was still about 8 per cent of secured debenture stock and was considered by the Board to be sufficient.

[120] When Bridgecorp collapsed in July, it was clear to the Board that the market place was becoming very volatile. Deposits had fallen due to a lack of confidence in finance companies. While some of the projects being funded had still to reach completion, there was evidence as the year progressed that refinancing was becoming difficult and sales were slower than expected. Sir Douglas saw this as a downturn in the market and did not regard it as a crisis. Nevertheless, as cash was being used to repay maturing deposits, and with new or reinvested deposits reducing, Sir Douglas said the increasing importance of loan repayments was obvious to all.

[121] Sir Douglas detailed the steps taken to monitor loan repayments including the formation of the large loans committee. He acknowledged concerns about the

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[53] Lombard Financial Services Ltd.

Brooklyn loan and expressed relief when the project was purchased by Mr Manning in November 2007. He spoke at seminars held in September to appraise investors of the company's position. Investors were assured that Sir Douglas and the other directors continued to be confident about the strength of the company. However, if the market deteriorated further, the intention was to continue to carefully manage down the loan book over time and to pay out investors. Investors were also assured that, on current indications, they were likely to be paid in full with a residue available to shareholders. While speaking positively about the company, Sir Douglas also acknowledged the reality of the challenging market conditions.

[122] The Ferrier Hodgson report in September 2007 provided some comfort to the Board. It did not contain anything that the company was not already aware of. The Board noted Ferrier Hodgson's belief that the projections of cash flows prepared by the company's management did not appear to be unreasonable.

[123] As to delays in repayments, Sir Douglas accepted that repayments did not occur as forecast but pointed out that the liquidity profile was being constantly monitored by the Board which considered that the forecasts received were realistic. The impact of delays, when known, was reflected in the forecasts received and frequently refreshed on the basis of updated information. The cash flow forecasts, notwithstanding the variances, indicated that the company would have sufficient cash to meet all its obligations. The worst case scenario projection, while a prudent one to carry out, was not regarded as a realistic forecast of what would actually occur. Although there were delays in receiving loan repayments, the Crown's case had failed to acknowledge that between September 2007 and March 2008 the company had received about $14 million more in deposits than had been estimated by Ferrier Hodgson. It was acknowledged that liquidity was expected to be tight up to March but the projections showed that the cash balance would improve thereafter.

[124] While Sir Douglas was concerned about the apparent hardening of international economic conditions, this did not lead him at any stage prior to Christmas 2007 to doubt that the loans would be repaid, given time. The catastrophic economic events in the United Kingdom and the United States thereafter could not have been predicted at the time the amended prospectus was issued.

[125] Sir Douglas' evidence was that he believed at the time the offer documents were issued that they were true and continued to hold that belief until it became clear in early April that some loans might be impaired and that cash had fallen to critical levels. The return to a more stable economic situation the Board had expected did not happen.

[126] No concerns had been raised by Mr Foley, who advised Lombard in relation to the offer documents. In relation to the extension certificate, Sir Douglas was satisfied there had been no material deterioration in the company's financial position since March 2007. Indeed, he considered the company's position had improved since that date based on its net profit, a reduction in the amount owing for secured deposits, the amount outstanding under the loan book and an increase in equity. He acknowledged that, against those factors, repayments were very slow reflecting a hardening market and that it was obvious that, if the slowing of repayments continued, there would be pressure on liquidity.

[127] Sir Douglas' views on the relevant statutory duties were expressed in these terms:

> This statutory duty to act in the best interests of the company, and in this context its investors, had the potential to exist rather uncomfortably with the statutory duty not to mislead potential investors. However while the first could never be used as a reason not to comply with the second, in my opinion it did justify the conclusion that, unless there was compelling objective evidence of serious impairment or potentially insufficient cash to such an extent that the company could not responsibly continue to trade, [Lombard] should continue to trade. I considered that, apart from information that was required by statue [sic] to be disclosed, there was nothing that needed to be reported to investors or the market unless such evidence existed and was known to the Board. I knew that the shareholders would have to bear any loss up to the equity of $30m before any investor's capital would be at risk, and I thought the likelihood of that happening was very remote…
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> To act prematurely before becoming fully informed, could well have had disastrous consequences for our existing investors who might later have been able to claim this action had not been necessary in the first place and they had suffered losses which could have been avoided.

[128] Mr Jeffries and Mr Bryant gave evidence along similar lines. Mr Jeffries elaborated upon his role as chair of Lombard's audit committee and Mr Bryant spoke of his involvement as a member of the large loans committee chaired by Mr Wallace

(whom he regarded as having considerable expertise in the finance sector). The latter role involved close involvement with Lombard's executives who were regarded as competent and actively engaged in the management of the various loans. There was no suggestion of material impairment of loans despite delays in repayments. Such delays were regarded as an ordinary part of Lombard's business given that the borrowers were involved in property development. Mr Bryant also discussed his role as a member of the audit committee which met regularly with Lombard's internal and external auditors. No concerns had been raised about liquidity issues. He acknowledged concerns about the Brooklyn and Bayswater loans but received explanations he regarded as satisfactory.

[129] Mr Reeves gave evidence as Lombard's chief executive officer. He confirmed that in the first quarter of 2007, the Board had agreed with his recommendation to "hold onto funds and reduce lending". Up to about the middle of 2007 this had proved to be successful but, as time went by, the reducing loan book inadvertently increased the company's vulnerability to concentration risk. As the year progressed, the finance company market deteriorated in consequence of the failure of other finance companies and he began to look for alternative complementary business models and revenue streams. By September, the Ferrier Hodgson report recommended that Lombard focus on taking the remaining projects to fruition. The company's loan managers had been doing that continuously and successfully with other loans for the past five years.

[130] The amended prospectus was prepared not because it was required but because he wanted to disclose to investors that investor funds available to Lombard were being reduced; that the company was caught with a concentration risk on some of the remaining developments; and that the hardening market for finance companies was causing delays in settlement.[54] Advice was taken from Mr Foley and KPMG. Neither expressed any concern about the contents of the amended prospectus which was subjected to close examination in consultation with the Ministry of Economic Development.

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[54] This evidence does not appear to be wholly correct since the company could not have continued to raise funds from the public on the basis of the September prospectus beyond 31 December 2007 as discussed at [15] and [16] above.

[131] Mr Reeves added that, by November 2007, Lombard was reporting to the Securities Commission, the New Zealand Stock Exchange, the company's auditors, the Ministry of Economic Development, the Reserve Bank and Perpetual. With the exception of the Reserve Bank, these reports were being provided on a weekly basis.

[132] He was satisfied after a full examination of the forecasts relied upon at the 19 December meeting and their underlying assumptions that the forecasts were realistic and achievable. As well, he said he was in dialogue with Lehman Brothers about a possible joint venture and with Fortress (a US-based private investment company) with a view to possible alternative funding.[55]

[133] The directors' evidence was supported by the company executives and other witnesses identified at [55] above and by the expert evidence of Mr Appleby. In his view, the actions of the directors during 2007 were an appropriate response to the tightening market conditions experienced during that year. These included the decision to reduce the loan book in an orderly manner, the setting up of the large loans committee to manage the company's major loan exposures, the preparation of regular cash flow projections responding to changing conditions as they occurred, and regular and full reporting of Lombard's executives to the Board.

[134] Mr Appleby considered that the Crown had placed undue weight on the forecast milestones referred to by Ferrier Hodgson in their September report, noting that variances were to be expected in the dynamic business environment in which Lombard and other finance companies were operating. There was nothing to suggest that any of the major loans were impaired as at the date the amended prospectus was issued and therefore the cash flow projections produced at that time were appropriate.

[135] Mr Appleby outlined the dramatic events which unfolded in 2008 in the United States and in Europe leading to the global financial crisis. In his view, these could not have been anticipated by Lombard's directors at the date the amended prospectus was issued. There was, he said, a reasonable expectation that payments would be received from the Blue Chip group which would have enabled Lombard to

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55 In the end these prospects were not taken up and were overtaken by other events post-Christmas.

manage its ongoing commitments through to March 2008.[56] Although a reduction in the cash position was forecast at that time, this was expected to recover throughout the remainder of the 2008 year as the proceeds from other developer loans became available. While there had been a reduction in cash reserves, these had been used to repay Lombard's investors.

[136] Mr Appleby also criticised the methodology adopted by Ms Peden in her schedule. He did not consider it was helpful in a business like Lombard's to analyse the percentage discrepancy between forecast repayments and what was actually achieved. The Ferrier Hodgson report clearly envisaged there would be variances in relation to projected milestones. The timing of repayments would depend upon the completion of developments and matters such as the issue of code compliance certificates. He instanced a delay in receiving a payment from one of the borrowers (Der Rohe Holdings) caused by a hold-up of several months in obtaining the relevant certificate. And he pointed out that, at the time of the Ferrier Hodgson report, the $10 million expected from the purchase of the project by Mr Manning's group was to be readvanced to other interests associated with Mr Manning. He agreed it was important that the project milestones be carefully monitored but considered this was being carried out appropriately by Lombard's executives.

[137] Mr Gray's evidence was also important to the appellants' case. We discuss it below when dealing with Ms Peden's analysis.

The appellants' submissions

[138] Under this ground of appeal, Mr Farmer summarised the appellants' submissions:

- The amended prospectus accurately warned potential investors of Lombard's liquidity risk, both in relation to the finance company sector generally and in relation to Lombard in particular.
- The omission of the specific matters which the Judge said should have been disclosed did not render the amended prospectus misleading.

[56] A point strongly disputed by the Crown.

- Disclosure in the form the Judge suggested would have itself been misleading.
- The Judge's adoption of Ms Peden's analysis was wrong.
- The Judge failed to consider the unforeseen events of February/March 2008 which were submitted to be the real reason for Lombard's failure. Had the Judge done so, he would necessarily have concluded that the statements in the amended prospectus were not misleading.

[139] The written and oral submissions presented on behalf of the appellants were wide ranging and referred in great detail to the documentary and other evidence at trial. Effectively, we were invited to retry the appellants, contrary to the proper approach in criminal appeals. Mr Farmer drew our attention to the defence evidence called at trial, much of which we have already summarised, and highlighted a number of other issues including:

- The relative strength of the Lombard Group's balance sheet.
- The conservative approach he submitted had been taken to the cash flow projections (particularly to take account of the drop in investment and reinvestment rates).
- The directors' confidence in the competence of the company's management and in their projections based on past performance.
- The fluctuations that necessarily occurred in the cash balance which, he submitted, were not out of the ordinary.
- The directors' confidence that the company had sufficient resources to meet its obligations as they fell due.

Discussion and decision

[140] The focus of the inquiry at trial was whether the amended prospectus included an untrue statement or statements. In the present case, the Crown's allegation was that the amended prospectus was misleading by reason of the omission of particulars that were material to the statements it contained in the form and context in which those statements were made. On appeal, the question for us is whether, having regard to all the evidence, the Judge could reasonably have been satisfied to the required standard that the appellants were guilty. Despite the full submissions made by counsel, we are satisfied that the verdicts the Judge gave were

open on the evidence and that he could reasonably have been satisfied beyond reasonable doubt of their guilt.

[141] We accept that the amended prospectus gave considerable detail of the nature of Lombard's business, the risks investors faced and the measures taken by the company to manage those risks. It also advised investors that the company was experiencing reduced levels of reinvestment, that sales of properties were delayed, and that market confidence in the finance sector had decreased and might decrease further if there were failures of other finance companies. Investors were also advised there had been a reduction in current loans and that a period of constrained liquidity would impact on the company's future growth and profitability.

[142] Nevertheless, while warning of those risks, the amended prospectus went on to say that:

> The Board remains confident that, based on a range of conservative scenarios, Lombard Finance will have the required cash resources to fund all repayments to investors when due and that are not re-invested.

[143] The implication of the bolded passage in the amended prospectus which we have cited at [57] above is that Lombard would only be unable to meet its repayment obligations if the reduction in the level of reinvestment was extreme. In fact, that was not the only reason Lombard would not be able to meet its obligations.

[144] The general tenor of the amended prospectus, in particular the passages referred to in [142] and [143] above, was that despite current difficulties the directors were confident that Lombard could meet its obligations. We agree with the Judge that this did not sufficiently or accurately convey to investors the vulnerable state Lombard was actually in nor the level of the directors' concerns about that.

[145] Eliminating any issue of hindsight and focusing particularly on the contemporaneous documents and undisputed facts, there had clearly been rising levels of concern by Lombard's executives and directors for at least nine months prior to the issue of the amended prospectus on 24 December 2007.

[146] From March, the company had decided not to make any new advances, to focus on recovering existing loans, and to ensure there was a sufficient cash balance to meet repayment obligations to investors. The large loans committee was established in May.

[147] Then, in July and August Bridgecorp and Nathans Finance collapsed. This clearly sent shockwaves throughout the finance sector and the business community more generally. Concerns by Perpetual as statutory trustee led it to require Lombard to obtain an independent report from Ferrier Hodgson who reported in September.

[148] We have summarised the contents of this report at [36]–[42] above. It is sufficient to note here Ferrier Hodgson's description of the company as being in "running down" mode (a fact not conveyed except by the reference to the reduction of the loan book over the 12 months to September 2007); the fact that reinvestment rates had "plummeted"; the importance of loan repayments being received when projected; and the need to retain a cash buffer to ensure the company's liquidity.

[149] By November, there was even more serious concern by the directors. Unusually, three of them were present at the meeting of the large loans committee on 15 November. The extent of Sir Douglas Graham's concerns are reflected in the email he sent the same day to Mr Reeves.[57] Sir Douglas explained in evidence that his remark about the company now sailing very close to the wind did not mean the company was in crisis, but the terms of the email speak for themselves. In saying that, we imply no criticism of Sir Douglas who was properly concerned not to be a party to any misleading of the public. But we agree with the Judge that the failure of the amended prospectus to disclose the extent of the directors' concerns about the company's liquidity was a material omission that resulted in the statements in the prospectus about the directors' confidence in the company's ability to meet its commitments being materially misleading.

[150] Between August and December, the cash on hand had steadily deteriorated from the highs of $39 million in August and $33 million in September when Ferrier Hodgson reported, to $7.2 million at the date of the Board meeting on 19 December.

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[57] Quoted at [49] above.

There can be no doubt from Ferrier Hodgson's September report and the subsequent documentary evidence that the existence of an adequate cash buffer was regarded as important by the directors. The fact that it had deteriorated sharply since August/September despite the intensive efforts made by the company to recover the loans outstanding was a material fact that was not disclosed.

[151] We accept Mr Farmer's point that the cash reserves in August/September were unusually high but we do not view that as detracting in any significant way from the Judge's conclusion that the company's cash reserves had deteriorated substantially from just after mid-year and were continuing to do so. It is important to recall that the levels of cash reserves had been deliberately increased by the company for the very purpose of providing a cash buffer in straightened conditions. The importance of an adequate cash reserve continued to be a focus for the appellants and Lombard's management.

[152] We agree with Dobson J that it was not necessary and probably not desirable, given the fluctuating nature of the cash at bank, for the amended prospectus to state what the actual cash figure was at that time. But we also agree with the Judge that this did not relegate the trend in the company's cash position to immateriality given its importance by December 2007 to the company's liquidity. The failure to identify this trend was, by itself, a material omission that rendered the statements about liquidity in the amended prospectus misleading and therefore untrue.

[153] It was entirely open to the Judge to conclude that the amended prospectus omitted to convey the extent of the discrepancies between the forecast timing of loan repayments and their actual receipt.[58] Mr Carruthers emphasised that the company's cash flows adopted by Ferrier Hodgson in September had projected recoveries of $49.89 million by the end of December, yet only $22.463 million had actually been received by the end of November.[59] Of the $19.2 million later forecast to be received between 1 and 18 December, only $5.3 million was actually received prior to the 19 December Board meeting. Of the further $14 million expected to be

58 As noted at [114] above.
59 The $49 million of projected recoveries by end December represented about 35 per cent of the $140 million in total advances made by Lombard as recorded at the time of the Ferrier Hodgson report.

received on 19/20 December, only $5.2 million was received before the amended prospectus was registered on 24 December. According to Mr Cable's evidence, this resulted in a cash balance of only $8 million compared with the $17 million then projected. These facts are not disputed.

[154] The Judge relied in part on Ms Peden's schedule to support his conclusion that the amended prospectus ought to have included reference to the lack of reliable forecasts of the timing of loan repayments. Mr Farmer challenged the conclusions reached by Ms Peden. He did so substantially on the basis of criticisms which had already been made in the High Court. Although submitting that some of Ms Peden's base figures were wrong, Mr Farmer's major criticism was her methodology.

[155] At trial, the defence challenged Ms Peden's conclusions relying on analyses prepared by the accountant, Mr Gray. His view was that there were errors in Ms Peden's figures and in the methodology she applied in reaching her conclusion that there was a discrepancy between the forecast and actual loan repayments over the period September to December 2007 of 46 per cent. In summary, Mr Gray's main criticisms were:

- Cash received and re-advanced in relation to the Mahia Gateway development was wrongly excluded.
- In some cases there were "double-ups" in the amounts forecast to be due resulting from adding together repayments expected in successive forecasts.
- It was wrong to rely on a cumulative total by adding the forecast receipts in successive months.
- On Mr Gray's calculations, the equivalent results for the critical month of November 2007 were 87.8 per cent accuracy for loan repayments and 93.1 per cent for drawdowns. This compared with Ms Peden's figures for that month of 42.7 per cent and 64.1 per cent respectively.
- These differences had flow-on effects in relation to the calculation of the degree of inaccuracy in post-Christmas projections (although Mr Gray accepted that increased drawdowns would tend to offset errors in the alleged overstating of projected loan repayments).

[156] The force of the criticism about the Mahia Gateway payments was lost for two reasons. First, Mr Appleby agreed with the Crown that the Mahia payments

were appropriately excluded from its analysis. The Judge noted that the repayment and re-advance in relation to Brooklyn (for significantly larger amounts than those relating to Mahia) were also excluded.[60] Mr Gray had not contended for their inclusion. Second, the Judge also concluded (correctly in our view) that it was important to appreciate the rationale behind Ms Peden's analysis. This was to demonstrate the relative accuracy of management's projections as to loan repayments. The analysis was not intended merely to reflect the amounts of money being received and to set those off against the amounts paid out.[61] The other criticisms advanced by Mr Gray were primarily directed towards Ms Peden's calculations of the alleged inaccuracies on a cumulative basis, month on month.

[157] The Crown did not accept there was any double counting but was content to leave to one side the cumulative figures and simply work from a comparison of the average monthly forecasts versus the actual payments received. On that footing, Mr Gray accepted in cross-examination that Ms Peden's schedule showed that the forecast loan cash flows compared with the payments actually received showed that the average achieved for the months of September, October and November was 40 per cent (being 13.9 per cent, 36.4 per cent and 69.7 per cent divided by three) and, to the end of December, was 43.75 per cent. The average across the whole period to the end of March 2008 was 46 per cent. In agreeing that this was what the figures showed, Mr Gray did not accept their correctness. Nevertheless, they were accepted by the Judge.[62]

[158] In response to Mr Appleby's criticisms, the Crown submitted that Ms Peden's approach in analysing the forecast over the period September to December 2007 took into account the adjustments to the Ferrier Hodgson forecast made by the company on a monthly basis. As such, her analysis did not suffer from any defect in that respect. The Crown also pointed out that the analysis adopted by Ms Peden did not rely upon the tracking of actual performance against forecast in respect of particular loan repayments. Rather, it focused on the overall cash position of the company by reference to the total loan repayments forecast (from whatever source)

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60 At [101].
61 At [102].
62 As we have recorded at [62] above.

against the actual loan repayments received (irrespective of their source). This gave the true picture of the deterioration of the company's cash position caused by a failure to meet loan repayments. On this basis, the criticism of double counting was said not to be justified.

[159] Ms Peden's analysis was also relied upon to support the Judge's conclusion that the directors ought to have questioned the accuracy of management's cash flow projections. But we accept that it was prepared in hindsight and was not the sort of detailed analysis that the appellants could have been expected to undertake before issuing the amended prospectus.

[160] On the other hand, despite the possibility of some inaccuracies, the analysis was useful as illustrative of the extent to which loan repayments were not being met as forecast despite close monitoring and frequent adjustment of the forecasts to take into account changing circumstances as they arose. Importantly, the analysis identified in summary form what the directors already knew from the other information they had at hand at critical times. Independently of Ms Peden's analysis, the directors knew there were major discrepancies between the forecast repayments and the actual payments received. They also knew about the marked deterioration in the company's cash position as described at [153] above.

[161] While we accept delays in loan repayments were not uncommon in the type of business conducted by the borrowers, the delays in loan repayments and the extent of inaccuracy in the cash flow projections were very serious issues in the climate prevailing in the last quarter of 2007. The directors knew that Lombard's liquidity was critically dependent on the timely receipt of the loan repayments and that delays in receiving those payments were the prime reason for the significant and ongoing deterioration in the company's cash reserves.

[162] Whether or not the appellants ought to have questioned management more closely about the accuracy of the cash projections, the failure to inform investors that there were marked discrepancies in those projections constituted a material omission that resulted in the statements in the amended prospectus being untrue. As the Judge said the clear pattern of overstatement of projected loan recoveries was material to

potential investors as tending to demonstrate that market conditions were so unpredictable that cash flow projections could not reliably be made.[63]

[163] It was open to the Judge to conclude that the amended prospectus did not sufficiently convey any sense of how vulnerable the company was as at 24 December and how close it was to being unable to meet its commitments. It was not merely a question of whether the directors genuinely believed the company could survive despite the serious liquidity problems. Nor whether the directors believed the explanations given by management for the delays in payments to be reasonable. The real issue for the purpose of the charges the appellants faced was whether the statements in the amended prospectus were accurate without reference to the extent of the delays in receiving loan repayments and to the significant and ongoing discrepancies between the projected timing of the loan repayments and their actual receipt.

[164] We are satisfied it was open to the Judge to conclude that there was a sufficient pattern of delayed payments and of significant differences between the projected timing and receipt of payments to require reference to be made to this in the amended prospectus. Without such reference, we consider the amended prospectus was materially misleading.

[165] The minutes of the Board meeting on 19 December are relevant to this issue. Mr Beddie is recorded as frankly acknowledging that it would be a challenge to balance receipts and payments each month. Reference was also made to the Brooklyn and Bayswater loans. Although we acknowledge that repayments on those two major loans (totalling $50 million) were not included in the loan projections for that meeting as being recoverable in the short term, the expression of "hope" that those loans might settle early in 2008 was no more than that.

[166] We do not overlook that the Judge did not find that any of the loans were impaired in the sense he described (except in one immaterial respect) but the distinction between the ability in the longer term to recover the loans and the timing

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[63] See the quoted passage at [65] above.

of recoveries was a proper one to draw in relation to the key issue of Lombard's liquidity.

[167] Nor are we persuaded that the Judge was wrong to find that the appellants could justify omitting reference to the identified matters on the basis that the analysis of those matters was properly for the judgement of the directors. While we accept that directors must exercise a degree of judgement in deciding upon the wording of the offer documents and on issues of materiality, the statutory obligation is clear. The statements made must be true and must not omit any material matter that would render those statements misleading and therefore untrue. Ultimately, whether that has occurred is a matter for the court to determine but investors are entitled to make their own judgement on whether to invest on the basis that statements in the offer documents are true and not materially misleading.

[168] We have not thought it necessary or appropriate to analyse the events that occurred after Christmas 2007. While the indictment covered the period up to the company's receivership in April 2008, the primary focus was on the period up to 24 December when the amended prospectus was registered. Mr Farmer emphasised that the appellants could not have foreseen the major adverse events that affected all international economies in 2008 which led to the global financial crisis and what counsel described as the "bank lock-up". We accept that. But the storm clouds had clearly been gathering in New Zealand during 2007 and they intensified as the year progressed. Lombard's position in the last quarter of 2007 was far from "business as usual". The catalogue of events we have outlined (starting as early as March 2007) demonstrate plainly that Lombard was in an extremely vulnerable state. The directors knew that, yet failed to ensure that the amended prospectus spelled that out for investors.

[169] Mr Farmer also submitted that the events overseas in 2008 were the real cause of Lombard's demise. We do not propose to dwell on that submission since we do not regard it as material to our decision. The focus of the case was on the truthfulness and materiality of the statements contained in the prospectus at 24 December in the light of what was known or could have been reasonably

anticipated at that time. What might ultimately have caused Lombard's collapse has no relevance to that issue.

Conclusions

[170] Our overall conclusion is that, on the basis of all the evidence available to the Judge, it was entirely open to him to conclude that the statements in the amended prospectus were untrue by the omission of reference to

- The sharp deterioration in the company's cash position.
- The serious downward trend in the company's cash position.
- The pattern of serious delays in the recovery of loan repayments.
- The significant discrepancies between the projected timing of loan repayments and their actual receipt.
- The extent of the directors' concerns about these matters.

[171] All of these matters were critical to the liquidity of the company and its ability to meet its commitments when due. The omission of reference to these matters meant that the amended prospectus did not convey the imminence of the identified risks and the vulnerable state the company was actually in. We are satisfied the Judge was right to find these matters were material to investors and that, without reference to them, the statements in the amended prospectus were misleading and untrue. It was not necessary for the Judge to identify precisely how these matters should have been expressed in the amended prospectus. It was sufficient to identify the topics that ought to have been included and the general nature of them.

[172] We wish to add a point about the concern expressed by the directors that the inclusion of more material in the amended prospectus might have led to the premature demise of the company. When a public offer is made, the statutory obligation is to ensure that the statements made in the offer documents are true and that they are not rendered untrue by material omission. That obligation overrides the duty directors owe to the company to act in its best interests (where those duties may conflict). It also means that if the directors cannot be satisfied that the statements

contained in the offer documents are true and are not misleading by omission, the offer should not be made irrespective of the consequences that might then flow. Decisions on issues such as this can be finely balanced but it is the directors' role to make them nevertheless.

[173] In this respect we agree that the obligations of directors under the Act are non-delegable and cannot be avoided by reliance on information supplied by management.[64]

Third ground of appeal – misdirection in relation to the statutory defence under s 58(4) of the Act

The Judge's findings

[174] For convenience, we set out s 58(4) again:

> (4) No person shall be convicted of an offence under subsection (3) of this section if the person proves either that the statement was immaterial or that he or she had reasonable grounds to believe, and did, up to the time of the distribution of the prospectus, believe that the statement was true.

[175] The Judge was not satisfied on the balance of probabilities that the appellants had shown that they had reasonable grounds to believe, and did believe, that the statements in the amended prospectus were true so as to give them a defence under s 58(4) of the Act. The findings by the Judge on this issue were challenged on the grounds of misdirection as well as more broadly on the grounds of unreasonable verdict. It is convenient first to set out the Judge's findings.

[176] The Judge summarised his findings in these terms:

> [125] I am satisfied on the balance of probabilities that each of the accused considered that the statements addressing the company's liquidity in the amended prospectus were true at the time it was issued. They had confidence in the respective loan managers providing the forecasts for loan repayments in and after December 2007. The accused considered that the loan managers had an established track record of expertise, and that the explanations provided by them for non-compliance with projections over the preceding months were reasonable.

[64] See the useful discussion by Heath J in *R v Moses*, above n 15, at [74]–[87] and our further observations at [196] below.

> [126] However, the accused's approach depended on their view that monitoring the accuracy of loan repayment projections was a matter of detail on which investors would trust the directors' judgement. I do not find that a sufficient approach to justify the omission of any reference to the relative inaccuracy of such projections as "reasonable". The timing of loan repayments was critical, and adequately informed investors could well take a different view from the directors about the extent of risk that arose from reliance on those projections. It was not reasonable for the accused to take the view that they could leave readers of the offer documents in the dark on that matter.
>
> [127] Similarly, on the omission of any reference to the trend of reduced cash on hand, and the level of the accused's concerns over liquidity. In essence, the accused's claim to reasonable grounds for the belief that their concerns did not need to be acknowledged depended on their view, to the effect that "yes, it's likely to be very tight and we are worried about it, but we think we'll squeeze through, so we needn't raise unnecessary concerns". Readers of the offer documents ought not to have been reliant on directors' judgement on that matter, and I am not persuaded that it was reasonable for the accused to believe that they could omit any such reference.

[177] The Judge went on to consider three other related matters. First, he considered and rejected a submission by the Crown that the appellants had not given adequate consideration to the content of the amended prospectus. Second, the Judge rejected a submission made by the appellants that their assessment of what had to be disclosed in relation to investment risks was, in a commercial sense, influenced by their obligations to existing investors and possibly the shareholders in Lombard's parent company. It had been submitted that the contents of the offer documents should not be any more pessimistic about risk when, to do so, might jeopardise Lombard's ongoing business. The Judge recorded that none of the appellants argued that the balance between full disclosure and protecting the ongoing business could affect an analysis of the extent of disclosure required in order to ensure that the offer documents were not misleading. However, it was suggested, the Judge said, that the dilemma in balancing these different interests affected the reasonableness of the directors' belief as to the adequacy and accuracy of what was stated in the offer documents.

[178] The Judge firmly rejected this proposition:

> [137] I do not accept that the interests of existing investors, be they the holders of debt securities or shareholders, can validly be taken into account in assessing the reasonableness of views formed by the directors as to the absence of any misleading content in the offer documents. The standard imposed by s 58 of the Act is absolute in the sense that criminal liability will

> follow from the issue of documents containing untrue statements or omissions. The statutory defence of reasonable belief in the truth of content is not a variable standard of reasonableness, depending on other pressures acknowledged by directors in forming the views that they do.

[179] We agree entirely with the Judge on these points.[65]

[180] The Judge then addressed a third issue as to whether the appellants could call in aid the fact that Lombard's professional advisers had not raised any issues about the content of the prospectus. The Judge noted that the company's auditors had a measure of involvement in settling the form of the company's financial statements for the six months to 30 September 2007. However, the accounting firm involved had no audit responsibility for those statements. Their involvement in the last quarter of 2007 had not provided any opportunity for them to express a view about the company's financial health.

[181] Reliance was nevertheless placed by the appellants on the absence of any warning signals from the auditors, the statutory trustee or the Companies Office responsible for considering the content of offer documents. As well, the appellants relied on Mr Foley's evidence that the level of disclosure in the offer documents exceeded industry norms at the time. The Judge accepted that if Mr Foley had urged greater or different disclosure, the appellants would have followed such advice.

[182] After considering these issues, the Judge concluded:

> [145] Certainly in the negative sense, had the accused proceeded to issue the offer documents whilst a professional adviser questioned the need for different or additional content, then that would adversely affect the reasonableness of their belief in the accuracy of the offer documents. I am not satisfied that the same relevance can be attributed in the positive sense to the absence of warning signals from competent external advisers, as supporting a positive finding that there were reasonable grounds for the directors' belief in the accuracy of the offer documents. The directors' obligations in relation to the accuracy of content of offer documents are non-delegable. As a matter of context, I accept that where [Lombard] retained competent outside advisers, respected their views, and completed the offer documents without those advising [Lombard] raising any relevant concerns, that it is marginally easier for the accused to make out reasonable belief. It would not, however, be sufficiently material to establish a basis for reasonable belief, if it did not independently exist.

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[65] See also our discussion at [172] above.

The appellants' submissions

[183] The proposition advanced in support of the misdirection ground of appeal was that, instead of asking the statutory question whether the appellants had reasonable grounds to believe, and did believe, that the statements in the prospectus were true, the Judge asked a different question, namely whether the omission of the identified material was reasonable from the point of view of potential investors deciding whether to invest in Lombard.

[184] In support of this submission counsel referred to the Judge's observation that it was not reasonable for the appellants to take the view that they could leave readers of the offer documents "in the dark" on issues such as the timing of loan repayments, the trend of reduced cash on hand and the level of concerns held by the appellants over Lombard's liquidity.[66] Reference was also made to another passage in the judgment where, in summarising his findings, the Judge recorded that the appellants had not established "that it was reasonable for them to omit descriptions of the features I have identified, and that were known to them but not acknowledged in the offer documents".[67]

[185] In developing this submission, counsel referred to the decision of the Supreme Court of Canada in *Sharbern Holding Inc v Vancouver Airport Centre Ltd*.[68] The Court was considering an appeal relating to an alleged failure by Vancouver Airport Centre Ltd to disclose differences in financial arrangements given to the owners of two separate hotels being developed on the same property. Reliance was placed on two statutes in British Columbia: the Securities Act, RSBC 1996 and the Real Estate Act, RSBC 1996. Under s 75 of the latter, the developer could be liable to compensate purchasers if the prospectus or disclosure statement contained any material false statement unless it is proved:

> … that, with respect to every untrue statement … the person had reasonable grounds to believe and did, up to the time of the sale of the [land] … believe that the statement was true …

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[66] At [126] and [127].
[67] At [330].
[68] *Sharbern Holding Inc v Vancouver Airport Centre Ltd* 2011 SCC 23, [2011] 2 SCR 175.

[186] In dismissing the appeal and finding in favour of Vancouver Airport Centre, the Court found that the absence of the information identified was not material. The appellant had not demonstrated that "there was a substantial likelihood that disclosure of the [relevant material] would have assumed actual significance in a reasonable investor's investment decision".[69] Addressing the statutory defence under the Real Estate Act, the Supreme Court said that:[70]

> … To rely on the defence, [Vancouver Airport] had to show (1) that it subjectively believed the representations it made were true, and (2) that it objectively had "reasonable grounds" for such a belief. In considering the defence, the question is not whether [Vancouver Airport's] conclusion itself was reasonable. Rather it is whether [Vancouver Airport] subjectively believed its representations, and whether that belief had an objective basis in the sense that there were reasonable grounds for the belief.

[187] It was argued for the appellant that the proper test focused on the objective reasonableness of the appellants' belief in the truth of the statement, notwithstanding the omission. The Judge had not addressed this question. Rather he had asked whether it was reasonable to omit the reference to the matters the Judge had identified. Counsel submitted this was a fundamental error since the Judge had already found that it was not reasonable to omit the identified matters. Having reached that conclusion, the Judge was unlikely to conclude that the statutory defence was available.

Discussion

[188] In a case where the prosecution relies on untruthful statements as a result of material omissions, the test to be applied in relation to the statutory defence under s 58(4) is whether the appellants believed the statements in the amended prospectus were true despite the omissions identified and whether they had reasonable grounds for that belief. Given the finding by the Judge that the appellants did believe the statements in the amended prospectus were true despite the identified omissions, the only question for the Judge was whether the appellants had reasonable grounds for that belief.

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[69] At [91].
[70] At [92].

[189] Despite some infelicities of language, we are not persuaded that the Judge misunderstood the correct statutory question. The reference to leaving readers of the offer documents in the dark and the finding by the Judge that it was not reasonable for the appellants to believe they could omit the identified material must be read in context. While accepting that the appellants subjectively believed the amended prospectus was true without the omitted information, the Judge considered their belief was not based on objectively reasonable grounds. The Judge found that, given the information available to the appellants, it was not reasonable for them to conclude that monitoring the accuracy of loan repayment projections was a matter of detail on which investors would trust the appellants' judgement. This could not therefore provide a reasonable basis for the appellants' belief that the amended prospectus was true, without the omitted material.

[190] In support of his conclusion that there could be no reasonable basis for that belief, the Judge observed that the timing of loan repayments was critical and that adequately informed investors could well have taken a different view from the appellants about the extent of risk that arose from reliance on the cash flow projections.[71] The Judge made similar observations about the omission of any reference to the trend of reduced cash on hand and the level of the appellants' concerns over liquidity.[72] In those respects, the Judge said that readers of the offer documents ought not to have been reliant on the directors' judgement.

[191] We are satisfied that the Judge understood that these matters were to be considered in relation to the appellants' defence of reasonable belief in the truth of the offer documents despite the omissions.[73]

Fourth ground of appeal – the finding that the appellants had not established the defence under s 58(4) was unreasonable and could not be supported having regard to the evidence

[192] In their written submissions, the appellants submitted that the Judge had not properly identified and assessed the reasonableness of the grounds that the appellants

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71 At [126].
72 At [127].
73 See [128].

had for believing in the truth of the statements despite the omissions. Six principal grounds were relied upon by the appellants to support this submission:

- The Judge found that the loans were unimpaired and expected to be repaid in full.
- There was over $8 million on hand at the date of the amended prospectus which was sufficient to meet immediate interest and redemption obligations.
- The cash flow forecasts indicated there would be sufficient cash on hand to meet Lombard's obligations at least for the life of the amended prospectus.
- Even if there had been some impairment on the loans, or some unanticipated delay in payments, there was sufficient equity in the company to enable cash to be generated if required. In that event, any shortfall in cash would be borne by the shareholders rather than the investors.
- The appellants had taken professional advice which, while not exonerating them, was highly relevant as an objective fact supporting the reasonableness of their belief.
- The statutory trustee and the auditors had seen no reason to intervene.

[193] In oral argument, it was also submitted that the appellants were experienced and competent directors and that they were entitled to have confidence in the competence of the company's executives. It was also submitted that, for five years, Lombard had been profitable and was well managed. Although the $10 million which was expected to be paid upon the sale of the Brooklyn development to the Manning interests in November 2007 did not eventuate, the company expected that a larger reduction of the facility from refinancing would occur in early 2008. Otherwise projections were on track and sales of properties involved in other developments were proceeding.

Discussion

[194] While the appellants believed the statements in the amended prospectus were true despite the omissions of the identified matters, we are satisfied there was a substantial evidential foundation for the Judge to conclude that the appellants did not have reasonable grounds for that belief. It is unnecessary to rehearse in detail the

reasons for that conclusion. It follows inevitably from our discussion of the factual background at [25]–[53] of this judgment and our discussion of the reasons why there was a proper basis for the Judge to conclude that the statements in the amended prospectus were untrue by reason of omission. We have summarised those reasons at [140]–[173] of this judgment.

[195] In particular, the contemporaneous documentary evidence showed that the appellants were well aware of the three key matters the Judge identified: the serious delays in the recovery of loan repayments, the significant discrepancies between the projected timing of loan repayments and their actual receipt, and the obvious downward trend in the cash on hand. Importantly, the evidence showed that the appellants knew that these matters were critical to the liquidity of the company and had serious concerns in that respect. Yet the amended prospectus did not sufficiently convey any of these matters.

[196] Given the appellants' own knowledge of the critical state of Lombard's liquidity, neither reliance on the views of the company's executives nor the advice of professionals could avail the appellants. It was open to the Judge to conclude they could not have had reasonable grounds to believe that their expressions of confidence in the company's liquidity were true without reference to the omitted matters which demonstrated clearly the vulnerable state the company was in. Nor could they have reasonably relied on the advice and assurances of management in the circumstances. That is because of the non-delegable nature of the duty imposed by s 58 and because the ultimate responsibility to govern and manage the company is theirs.[74]

[197] While directors are entitled to delegate management responsibilities to the company's executives, the prevailing conditions in the last quarter of 2007 and the obvious lack of reliability in the critical cash flow projections meant there was evidence from which the Judge could properly conclude that the directors could not reasonably rely on the executives' advice and were obliged to take a much more direct personal interest in the company's affairs than might have been the case in a

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74 *Mason v Lewis* [2006] 3 NZLR 225 (CA) at [83] and *Dairy Containers Ltd v NZI Bank Ltd* [1995] 2 NZLR 30 (HC) at 79.

more favourable market. Although Mr Foley's advice was a factor relevant to the existence of reasonable grounds of belief, it could not have been decisive in the circumstances. It is a reasonable inference that the directors had much more detailed knowledge of the company's affairs than Mr Foley possessed, or for that matter, the company's auditors or Companies Office personnel whose advice was also relied upon to support the appellants' belief that the statements in the amended prospectus were true.

[198] We conclude that there was a proper basis on the evidence for the Judge to find that the appellants had no reasonable grounds to believe that the statements in the amended prospectus were true despite the omissions.

Result of the conviction appeals

[199] For the reasons given, the appeals against conviction are dismissed.

The Solicitor-General's sentence appeals

Introduction

[200] The Solicitor-General appeals against the sentences imposed on the respondents on the grounds that they are manifestly inadequate. The key grounds for the appeals are:

(a) The Judge wrongly characterised the respondents' conduct as an error of judgement.

(b) The proper starting point for the sentences was imprisonment.

(c) The sentences imposed were inconsistent with sentencing principles and comparable authorities.

(d) The discounts given for reparation and personal factors were excessive.

[201] In summary, the Solicitor-General's submission was that the starting point for the non-executive directors should have been in the range of two to two and a half years imprisonment. However, since these were appeals by the Solicitor-General, the lowest possible starting should have been 18 months imprisonment. For the

respondents Sir Douglas Graham and Mr Bryant, the total discounts for mitigating features should not have exceeded 20 per cent and, in Mr Jeffries' case, should have been minimal. In relation to Mr Reeves, the Solicitor-General's submission was that the appropriate starting point was two years nine months imprisonment but, since this was a Solicitor-General's appeal, the lowest possible starting point was two years imprisonment. Any discounts for personal factors in his case should have been minimal.

[202] The overall submission by the Solicitor-General was that sentences involving a combination of home detention and community work were appropriate, along with the reparation orders made in the case of Sir Douglas Graham and Mr Bryant.

The Judge's approach to sentencing

[203] After delivery of the guilty verdicts, the Judge gave a provisional indication that the likely sentences would be community-based along with orders for substantial reparation. However, after receipt of pre-sentence reports indicating that some of the respondents might not be able to make any substantial reparation payments, the Judge issued a minute clarifying that submissions on behalf of the respondents ought to respond to the Crown's submission that custodial sentences were appropriate.

[204] The Judge began the sentencing of the respondents by referring to the high importance of adequate disclosure that had been part of securities law in New Zealand since 1978. The Board would have been well aware of the provisions of the Act since both Sir Douglas Graham and Mr Jeffries had, in earlier years, had responsibility for the administration of the Act in their capacities as Minister of Justice. The essence of the factual background adopted by the Judge for sentencing purposes is captured in the following passage:[75]

> [5] Your offending involved issuing offer documents that expressed your confidence that Lombard had, and would have, sufficient liquidity to meet its obligations as they arose. The reality was that the Lombard Board had serious and constant concerns at the liquidity squeeze confronting the company at the time. Further, in the months before December 2007, predictions of the level of loan repayments had been highly unreliable when Lombard depended critically on projections as to the level and timing of

[75] *R v Graham*, above n 3.

> major loan repayments in order to maintain its liquidity. You had decided over previous months to conserve liquidity as much as possible and in absolute terms the cash in the bank was showing a substantial and virtually uninterrupted downwards trend. The offer documents made no mention of these important factors. As a result, readers of the offer documents had to form their views about the liquidity risk they would expose themselves to on inadequate and misleading information.

[205] The Judge found that investors had subscribed for some $10.45 million of secured and unsecured debenture stock and capital notes in Lombard during the currency of the offer documents between 24 December 2007 and early April 2008. Of that amount, some $8.7 million amounted to reinvestment by existing investors, leaving a balance of $1.7 million by way of new investments. These amounts excluded the sum of $2 million of previously unsecured investment by the parent company in Lombard that had been converted to secured debenture stock in early April 2008.

[206] Although not referred to in the sentencing notes, the respondents do not dispute that, as at the date of Lombard's receivership on 10 April 2008, the company owed approximately $125 million to about 4,400 investors. The estimated recovery for secured debenture holders was unlikely to exceed 15–22 cents in the dollar and there would be no recovery for capital and subordinated note holders.

[207] The Judge drew attention to the very serious range of consequences for those who relied on the misleading offer documents as illustrated by some 39 victim impact statements. The majority of the investors were retired people who were critically reliant on the return of their investments. Predictably, the financial harm suffered by investors had led to emotional stress and potentially to depression.

[208] The Judge also noted that, on a broader front, harm had been done in an institutional sense to the community's confidence in savings and investment. The personal reputations of the respondents had meant that Lombard was trusted by many small investors in preference to other finance companies.

Non-executive directors – Sir Douglas Graham, Mr Bryant and Mr Jeffries

[209] The Judge recorded that the maximum penalties for the respondents' convictions were imprisonment for a term not exceeding five years or a fine not exceeding $300,000, plus $10,000 a day for continuing offences. The Crown had submitted that the appropriate starting point for the non-executive directors was between two and two and a half years imprisonment. In the case of Mr Reeves as chief executive, the Crown's submission had been that a higher starting point in the vicinity of two years nine months imprisonment should have been adopted.

[210] After reviewing sentences in comparable cases the Judge characterised the offending by the non-executive directors as a material misjudgement about the extent to which concerns about Lombard's liquidity, and factors materially contributing to that, should have been disclosed in the offer documents. The decision relating to these concerns was, however, not one the Judge found the directors could reasonably have come to. He accepted that the non-executive directors had acted honestly and had committed personal care and attention to the offer documents. The Judge did not accept the Crown's contention that the respondents had been guilty of a breach of trust in the sense that concept is used in the Sentencing Act 2002.

[211] In relation to a submission by the Crown that the respondents ought to have withdrawn the offer documents when it became plainly obvious by mid or late February 2008 that Lombard was in serious difficulties, the Judge considered there was some scope for the Crown to argue that the nature of the misleading or inadequate information conveyed by the offer documents was made worse by the passage of time. However, he considered the respondents' conduct post-December 2007 was not deserving of any material weight as an aggravating factor in assessing the relative seriousness of the offending.

[212] The Judge rejected the Crown's submissions on the starting point in these terms:

> [44] The Crown submissions on the starting point reflect an expectation that all convictions under s 58 involving misleading offer documents issued by finance companies where any degree of money subscribed and any degree of carelessness was involved will justify a starting point of imprisonment.

> That is not the case. In lesser cases of inadvertence or error of judgement rather than gross negligence, there will be cases where an appropriate response does not require a starting point of imprisonment. There will be some cases in which the appropriate starting point is on the cusp between a short sentence of imprisonment (which carries with it the prospect of home detention in substitution for imprisonment) and the community-based sentences that sit below custodial sentences in the hierarchy of sentences.

[213] The Judge then went on to consider issues of deterrence and denunciation. He took into account in the case of Sir Douglas Graham and Mr Jeffries that:

> [46] … the blight caused by these convictions on your previous good reputations as former Ministers of the Crown, holders of other public offices and leaders of your communities is measurably more punitive than for previously respected businessmen or professional advisers.

[214] The Judge was satisfied that the fact of convictions in the case of each of the non-executive directors was, of itself, a more potent form of deterrence and denunciation than the additional consequences following from whatever sentence was imposed. The Judge considered in the case of all three non-executive directors that the convictions would severely dent the good reputations each had previously enjoyed. He also saw the convictions for the offending as being a deterrent to others who took on the role of company directors. As the Judge saw it, the fact of the convictions was more important in this respect than the extent of the sentences.

[215] The Judge then expressed his conclusion about the starting point:

> [51] I am accordingly not inclined to treat the requirement for deterrence and denunciation as warranting any increase from what would otherwise be the appropriate starting point for your sentences. Having regard to all of these considerations, I see the appropriate starting point for the non-executive directors as being a combination of community detention and community work. The maximum period of community work to which I could sentence you is 400 hours. Having rejected any more restrictive sentence up the hierarchy of sentences as not being necessary, I treat a combination including community work as appropriate because, notwithstanding the concerns I have for the victims who invested during the period of the misleading offer documents, there is a sense in which such offending should be recognised as offending against the community, and completing a sentence of community work will require each of you to confront some aspects of the community, as directed by those supervising your sentence.

[216] The Judge then considered aggravating or mitigating factors personal to the non-executive directors. He found no relevant aggravating factors. However, the

mitigating factors included their previous good character, remorse and, in the case of Sir Douglas Graham and Mr Bryant, their willingness to pay reparation. The Judge accepted that each of the non-executive directors had previously enjoyed widespread respect including recognition for significant public service in the case of Sir Douglas and Mr Jeffries. All three were persons of high personal integrity.

[217] In response to a submission by the Crown about the extent to which previous good character should be recognised when the existence of previous good character and reputation was relied upon in order to secure investments, the Judge accepted that the reputation of Sir Douglas Graham was a very important factor relied upon by Lombard's investors. Similarly, investors would have been comforted to a material extent by the additional assurance of Mr Jeffries' presence on the Board. In Mr Bryant's case, his professional and personal background similarly invited trust. On this topic, the Judge concluded:

> [64] Without downplaying the importance that good character and public service in previous life can have as a mitigating factor in sentencing, I am satisfied that it should not apply here to reduce the appropriate sentence to the full extent that exemplary character would otherwise attract, if the good character of the non-executive directors had not played such a material part in raising funds from the victims. Although your previous good characters are particular to each individual, in the end I can treat each of the non-executive directors in the same way on this point. I recognise your previous good character as a mitigating factor warranting a 15 per cent reduction from the starting point.

[218] The Judge accepted that Sir Douglas Graham and Mr Bryant had shown remorse, linked to their preparedness to pay reparation. But the Judge did not accept Mr Jeffries had demonstrated any remorse in a form that ought to be recognised as a mitigating factor on sentencing. No discrete discount for remorse was given in the case of either Sir Douglas Graham or Mr Bryant.

[219] As to reparation, the Judge noted that Mr Jeffries was not in a position to make any payment of reparation and, in any event, Mr Jeffries disagreed with the concept that sentences might be reduced through the payment of reparation. He had also resisted paying reparation because he did not accept that any conduct on his part caused any loss to the investors. The Judge rejected that proposition.

[220] The Judge considered other personal circumstances relating to each of the non-executive directors, including their age and state of health. He also noted that Mr Bryant had some serious health issues but all three were able to serve sentences of community detention and community work.

[221] The Judge was satisfied that the 15 per cent discount common to all three non-executive directors was sufficient to remove the requirement for a sentence of community detention and that the additional 25 per cent discount in the case of Sir Douglas Graham and Mr Bryant should be appropriately reflected in a proportional reduction of the length of a community work sentence. The Judge recognised this could not be measured by a purely arithmetical formula. Taking into account the total discounts applicable to Sir Douglas Graham and Mr Bryant (40 per cent in each case), and 15 per cent for Mr Jeffries, the Judge settled upon 300 hours community work plus reparation of $100,000 in the case of each of Sir Douglas Graham and Mr Bryant. The final sentence for Mr Jeffries was 400 hours community work.

Executive director – Mr Reeves

[222] The Crown submitted that Mr Reeves should be dealt with differently from the non-executive directors since he was the chief executive with day to day control of the management of Lombard and had a previous conviction in 2000 for breach of the same section of the Act. On that occasion, a fine of $1,000 was imposed. The Judge considered that these factors could "possibly" give rise to a short prison sentence which might be substituted with a term of home detention. As to mitigating factors, the Judge took into account Mr Reeves' expressions of remorse which he found to be closer to those of Sir Douglas Graham and Mr Bryant. Some credit was deserved for that. Some allowance was also made for good character. However, the Judge regarded the "overwhelming" mitigating factor in Mr Reeves' case as his state of health, the details of which we need not elaborate upon. Mr Reeves also had responsibility as the sole caregiver of two children and had partial responsibility for a third child.

[223] In the Judge's view, these factors justified a reduction from what would otherwise be the appropriate sentence which, the Judge considered, would be "beyond community based sentences". The Judge noted the Crown's acceptance that Mr Reeves' financial position was such that he was not able to pay substantial reparation.

[224] In the result, the Judge imposed 400 hours community work for Mr Reeves.

Overview of counsel's submissions

[225] Mr La Hood advanced the Solicitor-General's appeals on the basis that, notwithstanding some points of difference with sentences in the case of the directors of Nathans Finance and Bridgecorp, the Judge had erred in failing to adopt a term of imprisonment as a starting point. Denunciation and general deterrence were no less important for those with high public standing than for others convicted of misleading investors. Here, both the sums involved and the number of investors affected were substantial and there was also an element of breach of trust.

[226] There were other aggravating circumstances including the deletion of items from minutes of the final Board meeting of the company on 9 April 2008 (which it was submitted showed the directors were concerned about the risks of trading over the previous few months); a late decision to reinvest the $2 million in capital notes held by Lombard's parent company as secured debenture stock; and the failure by the directors to correct the amended prospectus or to decline to accept further investments even when the position of the company became clear. In that respect, the Crown submitted that the respondents must have appreciated by February 2008 that the financial collapse of the company was inevitable.

[227] For the respondent directors, Mr Corlett submitted that the sentences imposed in Nathans Finance and Bridgecorp reflected the more serious circumstances of those cases: he emphasised the directors' honest belief in the truth of the statements in the amended prospectus; the care taken over the wording of the risk sections of the offer documents; the professional advice obtained; and the absence of personal gain. He submitted that a prison sentence need not be an inevitable consequence of offending that was the consequence of an honest mistake. Deterrence was not necessary for

directors who took care in the contents of offer documents and, in future, conduct not involving intentional or reckless behaviour was likely to be decriminalised.[76]

[228] It was further submitted for the directors that the Board had acted appropriately in February 2008 by seeking an independent report from KordaMentha and by declining to accept further investments in early April; there was no evidence that the directors had deliberately preferred their interests over their duty; and suggestions of breach of trust were misplaced.

[229] We will deal with each of the Solicitor-General's grounds of appeal in turn.

Characterisation of the respondents' culpability

[230] Mr La Hood submitted that the characterisation of the respondents' culpability as a case of misjudgement was wrong. It was submitted that the conduct of the respondents was such that it should be characterised as a case of "gross negligence". This is a difficult submission to sustain given the Judge's findings that the respondents acted honestly at all times, genuinely believed that the statements in the amended prospectus were true, and that careful attention had been given to the contents of the amended prospectus, including taking legal advice. The Crown acknowledged that none of the respondents had personally received any financial benefit and that there was no element of related party lending which had been a feature of other cases.

[231] Having received a large volume of evidence over the course of an eight week trial and having the benefit of hearing oral evidence from each of the directors, the Judge was in the best position to assess their culpability. We are not prepared to differ from his assessment on this point.

The starting point and consistency of sentencing

[232] We combine these two grounds of the Solicitor-General's appeals because we consider them to be closely related. A key factor in the sentencing of the

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[76] Citing the introduction in October 2012 of the Financial Markets Conduct Bill 2012 (342-2).

respondents and in the argument before us was a comparison of the sentences imposed on the directors involved in the Nathans and Bridgecorp cases.

Nathans Finance

[233] In Nathans Finance, four directors faced charges under s 58 of the Act. Mr John Hotchin pleaded guilty while Mr Kenneth Moses, Mr Mervyn Doolan and Mr Donald Young were found guilty after trial. The Solicitor-General has helpfully provided the following summary of the circumstances of the offending, the starting points adopted and the end sentences:

Summary				
Director	**Role**	**Circumstances**	**Starting Point**	**End Sentence**
John Hotchin	Non-executive director involved in both VTL[77] and Nathans	3 charges under s 58 of the Securities Act. Loss to investors $26 million, and indirect loss to economy. Not actual dishonesty. Untrue statements related to liquidity, bad debts, related party lending and credit assessment and management of loans.	3 years imprisonment	11 months home detention, 200 hours community work and $200,000 reparation
Kenneth Moses	Chairman	5 charges under s 58 of the Securities Act. Period of offending from 14 December 2006 to 20 August 2007. Losses to investors $66 million. Gross negligence rather than dishonesty. Untrue statements related to liquidity, bad debts, related party lending and credit assessment and management of loans.	3 years, 3 months imprisonment	2 years, 2 months imprisonment and $425,000 reparation
Mervyn Doolan	Executive director with day-to-day involvement in management of both Nathans and VTL		3 years, 4 months imprisonment	2 years, 4 months imprisonment and $150,000 reparation
Donald Young	Non-executive director without involvement in VTL		2 years, 9 months imprisonment	9 months home detention, 300 hours community work and $310,000 reparation

[234] In agreement with the Judge we accept immediately that the offending in the case of the directors of Nathans Finance was more serious than in the present case. Although there was no finding of dishonesty, when sentencing Messrs Moses,

[77] VTL was a party related to Nathans.

Doolan and Young, Heath J described their conduct as constituting gross negligence.[78] There had been a complete failure to perform their statutory functions as directors; there was no meaningful consideration of whether the offer documents were accurate; and there was undue reliance on professional advisors and senior management.

[235] We also accept there are further points of distinction in relation to the Nathans Finance sentencings. These include the wider scope of the omissions in the offer documents; the opportunities the directors had to correct the untrue statements; the duration the offer documents were in existence; the fact that substantial related party lending was involved; and the greater amount of the investments made during the period the offer documents were in existence.

[236] In sentencing Messrs Moses, Doolan and Young, Heath J considered that the primary sentencing goals were denunciation of the offending and deterrence of others from committing the same or similar offences. He agreed with observations made by Lang J[79] when sentencing Mr Hotchin that it was necessary to take into account that lack of trust would be likely to deter members of the public from placing funds with finance companies for a substantial period and to result in a reduction or removal of adequate venture capital from New Zealand capital markets.[80] As Heath J saw it, the purpose of denunciation and deterrence was to make sure that those who held office as directors and dealt with money provided by lenders of the public complied with their obligations to perform their functions to an appropriate standard. The Judge considered a firm sanction was needed.

[237] In Nathans Finance, the starting points adopted ranged from two years nine months to three year four months imprisonment. This Court later dismissed appeals by Messrs Doolan and Moses against their sentences.[81] The Court accepted that:[82]

> … such offending must be carefully analysed to determine the level of seriousness and the degree of culpability that a particular offender bears. Such offending will fit along the continuum from the most serious

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78 *R v Moses* HC Auckland CRI-2009-004-1388, 2 September 2011 at [16].
79 *R v Hotchin* HC Auckland CRI-2009-092-20927, 4 March 2011.
80 *R v Moses*, above n 78, at [26].
81 *Doolan v R* [2011] NZCA 542.
82 At [33] (footnote omitted).

> (dishonesty) to the least (which would include cases of innocent misrepresentation or lesser degrees of carelessness). We are satisfied it is not appropriate to draw bright lines between types of offending along the continuum. As the Judge remarked later, offending falling towards the top end of the gross negligence category will be akin to recklessness. Thus the different categories will tend to shade into one another.

[238] In the case of Mr Moses, this Court said that the starting point of three years and three months imprisonment chosen by the Judge was appropriate but added that "if anything, it was on the light side". Submissions that home detention might have been appropriate for both Mr Doolan and Mr Moses were firmly rejected.

Bridgecorp

[239] Mr Davidson was the chairman of Bridgecorp Ltd and Bridgecorp Investments Ltd. He pleaded guilty to 10 charges under s 58 of the Act. There was no suggestion of dishonesty. The loss to investors was approximately $119 million and the period of offending was from 21 December 2006 to 6 July 2007. The untrue statements in the offer documents were in respect of related party lending, credit policy, financial position and a statement that the company had never defaulted. In sentencing Mr Davidson, Andrews J adopted a starting point of three years three months imprisonment.[83] She imposed an end sentence of nine months home detention, 200 hours community work and made a reparation order for $500,000.

[240] The facts of Mr Davidson's case are perhaps the closest to the present case. Even so, we accept there are distinguishing features from the present case. These include the amount of the losses to investors in consequence of the offending, the wider scope of the untrue statements in the offer documents, related party lending and a longer period of offending. In deciding to impose a sentence of home detention, the Judge took into account his guilty pleas; his honest belief that the statements in the prospectus were true; the lack of any element of dishonesty or intentional wrongdoing; his distinguished career and high reputation in the legal profession; his genuine remorse; his co-operation with the authorities; and his offer to pay $500,000 in reparation.

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[83] *R v Davidson* HC Auckland CRI-2008-004-29179, 7 October 2011.

[241] These factors (other than the guilty plea) allowed the Judge to apply a reduction of 35 per cent, thereby adjusting the starting point to two years and one month imprisonment. A separate discount for the guilty plea further reduced the starting point to one year and eight months imprisonment. The Judge considered that home detention was appropriate and that this was the least restrictive sentence that could be imposed having regard to the statutory purposes of accountability, deterrence and denunciation and the importance of maintaining consistency in sentencing.

Other cases

[242] The adoption of starting points of imprisonment for offending against s 58 of the Act has continued to be the trend in the High Court since the present respondents were sentenced. In *R v Ryan*, Venning J sentenced three directors of Capital + Merchant Finance Ltd after they each pleaded guilty to two charges under s 58(3) of the Act and one representative charge under s 58(1).[84] The offending was more serious than the present case and the losses sustained by investors were substantially greater. The Judge also described the conduct of two of the offenders (Mr Ryan and Mr Sutherland) as approaching gross negligence. The Judge accepted they honestly believed the relevant statements were true but they did not have reasonable grounds for their belief. The third offender (Mr Tallentire) was much more intimately involved in the company's affairs and the Judge found he must have been aware of the falsity of the offer documents. Venning J adopted the following starting points and end sentences:

Offender	**Starting Point**	**End Sentence**
Mr Ryan	3 years imprisonment	7 months home detention 300 hours community work Reparation of $100,000
Mr Sutherland	2 years 9 months imprisonment	6 months home detention 300 hours community work Reparation of $60,000
Mr Tallentire	3 years 6 months imprisonment	12 months imprisonment cumulative on an existing sentence

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[84] *R v Ryan* [2013] NZHC 501.

[243] In *R v Banbrook*, Collins J imposed a sentence of eight and a half months home detention and ordered reparation of $75,000 after Mr Banbrook pleaded guilty to one charge under s 58 in relation to a prospectus issued by National Finance 2000 Ltd.[85] There were multiple false statements and the offending was over a period of nine months. Mr Banbrook's omissions amounted to gross negligence. The amount invested in reliance on the untrue statements was $2.35 million. The Judge accepted Mr Banbrook had been honest and that his offending arose from failing to make proper inquiries before the prospectus was issued. The starting point adopted was two and a half years imprisonment.[86]

[244] We also note an earlier District Court decision in *Ministry of Economic Development v Clegg* in which Judge Field sentenced the offender to 12 months home detention after he pleaded guilty to three charges under ss 58 and 59 of the Act and three under s 377 of the Companies Act 1993.[87] A starting point of two and a half years was adopted.

Starting point – discussion

[245] We accept that most of the cases to date reflect more serious circumstances and degrees of culpability than the present case but we are satisfied the Judge erred in adopting starting points short of imprisonment. There may be cases where culpability is properly assessed as being so low that a non-custodial sentence could be considered as the appropriate starting point. But this case does not fall into that category.

[246] First, the sentences needed to reflect the gravity of the offending.[88] By any measure, the number of investors affected, the serious impacts upon them, and the amounts of money invested or reinvested on the strength of the truth of the

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85 *R v Banbrook* [2013] NZHC 462.

86 Mr Banbrook's co-offender was sentenced by Toogood J in January 2012 (*R v Ludlow* [2012] NZHC 360) after pleading guilty to one count under s 58(3) and seven counts under s 51 of the Financial Reporting Act 1993 of knowingly making false statements. The starting point was four years imprisonment with an ultimate sentence of nine months imprisonment to be served cumulatively on a previous sentence. Both sentences are under appeal. Mr Banbrook has also appealed his conviction.

87 *Ministry of Economic Development v Clegg* DC Auckland CRI-2009-004-25176, 15 December 2009.

88 Sentencing Act 2002, s 8(a).

statements in the amended prospectus, were substantial. Second, while we accept the Judge's characterisation of the directors' culpability as a misjudgement, we cannot overlook the Judge's findings that the amended prospectus was misleading by omitting to identify the unreliability of the forecast dates for the known repayments, the serious deterioration in the company's cash resources, and the level of the directors' concerns about those matters. All these factors were critical to Lombard's liquidity at the time of a major tightening of the financial markets that gave rise to a string of corporate collapses and led the directors to place the company into "running down" mode. These factors clearly showed that the company was in a particularly vulnerable state yet these matters were not brought home to investors as they should have been.

[247] We are not disposed to accept the Solicitor-General's submission urging us to take into account the conduct of the directors after Christmas 2007 as discussed at [226] above. The primary focus must be on the position at 24 December 2007 when the amended prospectus was issued. We also accept Mr Corlett's submission that the breach of trust in this case is dissimilar from that in other cases in which such a breach is regarded as contributing to the culpability of the offender. The breach of trust in this case is better viewed as an aspect of the confidence the investors had in the directors by virtue of their reputation (particularly Sir Douglas Graham and Mr Jeffries but to a lesser extent also for Mr Bryant). This was a matter the Judge took into account in sentencing.

[248] However, we accept the submission made on behalf of the Solicitor-General that the Judge placed too little weight on the statutory purposes of denunciation and deterrence.[89] Much of the Judge's discussion on deterrence was focused on personal deterrence of the Lombard directors, the Judge accepting they were unlikely to re-offend. But, as Mr La Hood pointed out, the Solicitor-General does not contend that the sentence in this case needed to take into account personal deterrence. What was important was the need to deter others generally from offending in a similar way.

[89] Sentencing Act, s 7(1)(e) and (f).

[249] The Judge did not sufficiently focus on general deterrence and holding the offenders accountable.[90] The starting point ought to have reflected the purpose of the Securities Act, namely, to protect the investing public through the timely disclosure of material information.[91] The investing public is highly dependent upon the truthful disclosure of relevant information in offer documents. This is required to facilitate the raising of capital and to promote confidence by the investing public in financial markets. Failure to meet the required standards has a number of potential consequences: loss of investor confidence; a lack of trust in this country's financial institutions; damage to capital markets and the wider economy; and loss of funds invested by the public. Although the Judge noted some of these points, he did not give sufficient weight to them.

[250] We are satisfied these factors ought to have led the Judge to adopt a starting point of imprisonment in the case of each of the directors. To do so would have given effect to the important principle of consistency in sentencing.[92] The differences we have noted from the circumstances of the offending in Nathans Finance and Bridgecorp do not mean that a starting point short of imprisonment was appropriate. Rather, those differences should have led to a reduction of the starting point from those adopted in those cases.

[251] We consider that the starting point should have been two years imprisonment for the three non-executive directors (Sir Douglas Graham, Mr Jeffries and Mr Byrant) and two and a half years imprisonment for Mr Reeves as executive director. Any lower starting points would be manifestly inadequate. Given the long established principle that, upon a successful appeal by the Solicitor-General, a sentence is adjusted by no more than the minimum extent necessary to remove the element of manifest inadequacy,[93] we agree with the Solicitor-General's submission that the starting point should be adjusted to 18 months for the non-executive directors and to two years for Mr Reeves.

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90 Sentencing Act, s 7(1)(a).
91 See the discussion at [82]–[84] above.
92 Sentencing Act, s 8(e).
93 *Sipa v R* [2006] NZSC 52, (2006) 22 CRNZ 978 at [9].

Discounts for reparation, remorse and good character

[252] It was submitted for the Solicitor-General that the 25 per cent discount allowed to Sir Douglas Graham and Mr Bryant for the offer to pay reparation and remorse was excessive. Counsel observed that reparation is essentially compensatory in nature and is not intended to be punitive – discounts in excess of 10 to 15 per cent are rare. Discrete discounts for remorse are usually set at a low level and this was appropriate given that it was not until sentencing that remorse was expressed by Sir Douglas Graham, Mr Bryant and Mr Reeves.

[253] The Solicitor-General also submitted that the additional 15 per cent discount the Judge allowed for good character in the case of all three non-executive directors was excessive. It was submitted that the Judge did not make sufficient allowance for the fact that the investors had relied on the reputation of the non-executive directors in making their investments.

[254] Mr Corlett submitted that the discounts were appropriate. The Judge was obliged to take into account evidence of previous good character as a mitigating factor.[94] The appropriate discounts were properly within the discretion of the Judge who was in the best position to make the necessary assessment.

[255] We agree with the Solicitor-General that the total discounts of 40 per cent for Sir Douglas Graham and Mr Bryant were excessive. The allowance for the payment of reparation and remorse should not have exceeded 15 per cent.

[256] We do not accept the submission that no allowance should have been made for good character in a case where the reputation of the offender has been a material element in losses sustained by an investor. Sir Douglas Graham and Mr Jeffries were entitled to call upon their exemplary prior records and their service to the public. The misjudgement over the amended prospectus had serious consequences but they were entitled to have their previous good record taken into account. Similarly with Mr Bryant who was also entitled to rely upon his previous good character in mitigation of sentence.

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[94] Sentencing Act, s 9(2)(g).

[257] The reputation of the non-executive directors was undoubtedly an important factor in the minds of investors in Lombard but we do not see this as neutralising the previous good character the non-executive directors had in each case. Rather, it is a factor that should have led to some moderation of the overall discount for good character. In the circumstances, this should not have exceeded 10 per cent.

[258] It follows that the appropriate deductions should have totalled no more than 25 per cent for Sir Douglas Graham and Mr Bryant, and no more than 10 per cent for Mr Jeffries who had not offered to pay reparation and who had not accepted that his conduct had caused any loss to investors. The discounts totalling 40 per cent for Sir Douglas Graham and Mr Bryant were therefore manifestly excessive. The difference between 10 and 15 per cent for Mr Jeffries is of less significance and we are not inclined to treat it as a material factor by itself.

[259] In relation to Mr Reeves, Mr La Hood noted that the Judge had indicated that the appropriate starting point was quite "possibly" a short term of imprisonment but had not specified the length of the appropriate term. Unspecified reductions had then been applied for his ill health and for family reasons. The mitigating factors identified by the Judge in Mr Reeves' case related to a health condition and family responsibilities. As well, some remorse had been expressed although it is apparent this was a relatively minor factor in the Judge's assessment. As against that, there was Mr Reeves' previous conviction which the Judge did not view as carrying great weight.

[260] It is more difficult to make an assessment in Mr Reeves' case given the general terms in which the Judge expressed himself at sentencing. We accept that the Judge was entitled to take into account the factors he identified in mitigation of sentence. However, given the previous conviction, Mr Reeves was not able to rely on previous good character and we think some weight should have been given to the previous conviction as an aggravating factor, albeit that the previous offending does not appear to have been particularly serious.

Overall conclusion on the sentences imposed

[261] We are satisfied that the sentences imposed on each of the respondent directors were manifestly inadequate. The starting point should have been a period of imprisonment not exceeding 18 months in the case of the three non-executive directors (Sir Douglas Graham, Mr Jeffries and Mr Bryant) and not exceeding two years in the case of Mr Reeves as chief executive. Discounts for mitigating factors should not have exceeded 25 per cent for Sir Douglas Graham and Mr Bryant. Although we consider a discount of no more than 10 per cent was appropriate for Mr Jeffries, we would not regard the 15 per cent applied by the Judge as clearly excessive. For Mr Reeves, a discount for mitigating factors of up to 15 per cent could have been justified.

[262] By adopting a non-custodial starting point, the Judge did not give sufficient weight to the sentencing purposes of accountability, denunciation and general deterrence nor to the serious consequences to those who invested in reliance on the truth of the statements in the amended prospectus. The Judge also erred by failing to recognise the principle of consistency in sentencing.

[263] The adoption of a community-based starting point meant that a sentence of home detention was not available as a sentencing option.[95] Instead, the Judge imposed substantial terms of community work and, in the case of Sir Douglas Graham and Mr Bryant, ordered them to pay reparation of $100,000 each. We are satisfied that the least restrictive sentence having regard to comparable cases was a term of home detention combined with community work. A sentence of home detention reflects a perception that society's interests are better served in some cases by the imposition of restrictions on liberty through home detention rather than through imprisonment.[96] We are satisfied that the purposes of the Sentencing Act cannot be achieved by any less restrictive sentence.[97]

[264] We accept that if a term of home detention is imposed, the number of hours of community work ordered in the High Court should be moderated.

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95 Sentencing Act, s 80A.
96 *R v Hill* [2008] NZCA 41, [2008] 2 NZLR 381 at [33].
97 Sentencing Act, s 15A(1)(a).

[265] Prior to sentencing, reports were obtained under s 26A of the Sentencing Act about the availability of suitable addresses for the purpose of a home detention sentence. In each case, suitable addresses were identified although, in the case of Mr Jeffries, it was suggested there might be an issue with cell phone coverage. We propose to direct that updated reports be obtained solely to confirm the availability of suitable addresses for home detention. We will defer a final decision on the sentence appeals until those reports are received. The sentences of reparation imposed on Sir Douglas Graham and Mr Bryant are not challenged and will remain in place.

Outcome

[266] In formal terms:

(a) The appeals against conviction (CA191/2012, CA194/2012, CA201/2012 and CA204/2012) are dismissed.

(b) Leave to appeal is granted to the Solicitor-General in respect of appeals CA225/2012, CA226/2012, CA227/2012 and CA228/2012 but a final decision on those appeals is deferred until we have the further reports identified in (c) below.

(c) We direct that updated reports be provided to this Court as soon as possible for each of the respondents under s 26A of the Sentencing Act 2002, solely to confirm the availability of suitable addresses for home detention in combination with sentences of community work.

(d) The sentences of reparation imposed on Douglas Arthur Montrose Graham and Lawrence Roland Valpy Bryant remain in place.

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