	LCRO 25/2015
CONCERNING	an application for review pursuant to section 193 of the Lawyers and Conveyancers Act 2006
AND	
CONCERNING	a determination of a Standards Committee
BETWEEN	**LD AND KL TRUST**
	Applicant
AND	**MT AND HB**
	Respondents

The names and identifying details of the parties in this decision have been changed.

Introduction

[1] Mr LD has applied for a review of the determination by a Standards Committee to take no further action in respect of his complaints about the administration of [Company A]. He complains that the views of contributors were not canvassed as required by the Nominee Company Rules[1] and that the requirements of the Rules had not been complied with, resulting in loss to all contributors. Mr LD's complaint was lodged by Mr JK who had been instructed to make the complaint on behalf of Mr LD and KL Trust (the Trust).

Background

[2] The background information relating to this matter is well recorded in the Standards Committee determination and it is not necessary for me to repeat all of the detail.

[3] In June 2009 a proposal to invest in a mortgage was put before the trustees of the Trust. Mr LD was one of two trustees.

[4] The mortgage in which the Trust was being invited to invest was originally advanced in March 2007. The principal sum was $2,263,120 advanced to a company, [Company B]. The mortgage was secured over a property in [Location A] which the

[1] Lawyers and Conveyancers Act (Lawyers: Nominee Company) Rules 2008.

company intended to subdivide. The loan was guaranteed by the two directors of [Company B] ([Director 1] and [Director 2]) and was for a period of 12 months terminating on 29 March 2008. Interest for the term of the loan had been capitalised and retained by the nominee company. Ms BL, acting for Messrs MT and HB advises[2] there were about 50 contributors to the advance.

[5] The mortgage was renewed in 2008 with two new guarantors ([Guarantor 1 and Guarantor 2]) and one of the original guarantors was withdrawn.

[6] On renewal, [Company B] was to deposit the sum of four months interest in advance with [Law Firm A] with a further three months interest being payable on 1 August 2008 and 1 December 2008, with the final two months interest being paid on 1 February 2009. Mr MT advised contributors[3] that "the result of this is that the borrower will always be at least one month ahead in respect to payment of interest".

[7] Although it would seem that negotiations over the terms of renewal continued during 2008, the renewed term expired on 30 April 2009.

[8] The advance was not repaid when it fell due and negotiations commenced for a renewal for a further 12 months. At the time the Trust became a contributor in June 2009, the renewal terms had been agreed. The renewed term expired on 30 April 2010 and an amount equivalent to one month's interest was held by [Company A] as a "bond".

[9] The guarantors for the renewed terms were the original guarantors ([Director 1] and [Director 2]). In the application for review, Mr JK asserts that the guarantees from [Guarantor 1 and Guarantor 2] remained in place.

[10] The Trust invested $50,000 into this advance. It can only be assumed that this enabled an existing contributor to be repaid as there was no increase in the principal sum. The investment authority signed by the trustees is dated 6 June 2009.

[11] The first default occurred in January 2010 when the interest payment due was not made. That default was remedied but [Company B] subsequently defaulted in repaying the principal sum when it fell due on 30 April 2010. Between then and the sale of the property by [Company A] in November 2012, [Company A] sent 17 letters to contributors, the contents of which will be discussed later in this decision.

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[2] Letter BL to LCS (3 December 2013).
[3] Letter MT to contributors (6 May 2008).

[12] The sale by the nominee company resulted in a loss of $21,363.00 in capital by the Trust and $16,479.30 on account of interest.

Review

[13] This review has been completed on the papers with the consent of both parties on the basis that if the outcome of this review is to reverse or modify the Standards Committee determination, it would be forwarded to the parties in draft for comment.

[14] The draft decision was forwarded to the parties on 23 March 2016.

[15] In the course of the review a report was commissioned from Mr DS in which he was requested to advise what Nominee Company Rules were applicable (at the various stages during the term of the advance) and whether or not the applicable rules had been complied with.

[16] Mr DS was also asked to advise whether the loan was a "development mortgage" as that term is defined in both the Solicitors Nominee Company Rules 1996 and the Nominee Company Rules 2008.[4] Messrs MT and HB have acknowledged that the mortgage was a development mortgage as that term was defined in the 1996 rules[5] (the applicable rules). However, I agree with them and Mr DS that the mortgage was not one to which rule 8 of the 1996 rules applied as the advance secured by the mortgage was not applied (in whole or in part) towards the cost of the subdivision. Consequently, the restrictions imposed by rule 8 did not apply, and no consequences follow.

[17] Mr DS provided his report on 17 August 2015 and copies were provided to Mr JK and Ms BL under cover of a letter dated 21 August 2015. Ms BL provided comments on Mr DS' report by letter dated 1 October 2015 and Mr JK by letter dated 2 October 2015.

[18] Both the report and the reply comments have been considered by me in completing this review.

[4] Mr DS concluded while the advance was a development mortgage as defined in r 2.1 (1996 Rules) it was not a mortgage to which rule 8 applied, as the borrowed funds were not applied to the subdivision.
[5] Solicitors Nominee Company Rules 1996.

The DS report

[19] The report by Mr DS is comprehensive and addresses all of the issues which arise to be considered in the course of this review. Mr DS does not:[6]

> … believe that the causes of the failure of the mortgage, and the losses suffered by the complainant and the other investors, can properly be seen only in the context of the recovery action taken after the default occurred.

Mr DS structured his report to address the two distinct aspects of the history of the mortgage, the first being the formative circumstances of the investment, and the second being the actions taken by the lawyers following default.

[20] I must emphasise here that this review is not concerned with the causes of the failure of the mortgage, but the conduct of the lawyers. It is also important to note that the relevant conduct is the conduct of Messrs MT and HB at the time the Trust became an investor and subsequently when the mortgage fell into default. In this regard, I approach this review in the same manner that the Standards Committee approached the complaint, namely to examine the conduct of the lawyers "in the time period following when the Trust became an investor …"[7].

[21] I have adopted this approach, as the Standards Committee investigation did not proceed by way of an own motion investigation into the conduct of the lawyers prior to the Trust's involvement. If I were to focus on the conduct at the time of the inception of the loan that would be extending the ambit of this review beyond the investigation conducted by the Standards Committee and would require these aspects to be referred back to the Standards Committee pursuant to s 209 of the Lawyers and Conveyancers Act 2006. In this regard I am mindful of the comment by the Court in *Q v LCRO*[8] where the Court noted that the LCRO, having identified a mistaken perception by the Standards Committee, was not justified in "interfering in the decision and substituting her own views". Instead, the Court suggested that "even if the finding of a mistake had been well-founded, it is arguable that the proper course of action was for the Complaints Officer to have referred the matter back to the Standards Committee for reconsideration…".

[22] Mr DS' observations as to the commercial wisdom of the advance and the lack of attention to the financial strength of the proposal and of the guarantors, should not be ignored. I add to that, the number of "oversights" that occurred both on the setting

[6] DS Report (17 August 2015) at [2.4].
[7] Standards Committee determination (22 December 2014) at [38](2).
[8] *Q v LCRO* [2013] NZCA 570, [2014] NZAR 134 at [53].

up of this advance and subsequently. Mr DS' observations provide good lessons for those involved in nominee company lending. That includes all lawyers who are directors of nominee companies as required by the Rules (refer comments at [75] – [94]).

[23] I do not intend to take the step of formally referring these matters back to the Committee to consider, but either on an own motion, or as a result of a further complaint, the Committee may be required to consider these matters in due course.

Rule 13

[24] Rule 13 of the Nominee Company Rules provides:

> **13 Default procedures**
>
> 13.1 Each responsible lawyer must ensure that written notice in accordance with sub-rule 13.3 is given to each investor in a security as soon as is reasonably practicable on the occurrence of any of the following events:
>
> (a) default by the borrower for 30 days in payment of—
>
> (i) interest; or
>
> (ii) any part of the principal sum; or
>
> (iii) any other moneys due under the security; or
>
> (b) any other default by the borrower under the security unless the default does not materially affect the investors or the security.
>
> 13.2 Default by a borrower in payment of interest, principal, or other moneys due under the security must be notified, notwithstanding that the investors have received payment of the interest or other moneys by a guarantor or indemnifier, or a lawyer.
>
> 13.3 The notice under sub-rule 13.1 must—
>
> (a) specify the action the responsible lawyer is taking or proposes to take in respect of the default; and
>
> (b) request each investor forthwith to advise the responsible lawyer if the investor does not agree with the action or proposed action specified.
>
> 13.4 The responsible lawyer must determine the appropriate action to be taken in respect of any default, taking into account (as far as it is reasonable so to do having regard to the responsible lawyer's responsibility to all the investors in the security) the advice or instructions of each investor. Where the advice or instructions from investors conflict, the responsible lawyer must have particular regard to the advice or instructions of those investors who hold a majority in value of the principal sum secured.

> 13.5 In the event of a significant change in the action that a responsible lawyer is taking in respect of a default, where practicable a further notice must be given to investors as provided in sub-rule 13.3.
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> 13.6 The Law Society, on the application of a responsible lawyer, may grant such dispensations from this rule upon any condition or conditions that the Law Society in its absolute discretion may think fit to enable or facilitate the responsible lawyer to act to protect the interests of the investors in any security under which the borrower has made default.
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> 13.7 Each responsible lawyer must keep the investors reasonably informed as to the progress and results of the action taken by the responsible lawyer.
>
> 13.8 A responsible lawyer is not in breach of this rule if a default occurs that has not and could not reasonably be expected to become known to the responsible lawyer.

[25] Mr LD's complaint is that the letters sent to contributors did not include the specific request required by rule 13.3(b). Letters were sent on a regular basis to contributors following the defaults advising what steps the nominee company was taking to recover the money owed to the mortgagee. This commenced with reassuring statements following the initial default:[9]

> From our perspective, unless the default is remedied, we will move quickly to protect your interest by way of a mortgagee's sale. Given the ratio of borrowing to the valuation, we do not anticipate any losses should a mortgagee sale be necessary

[26] That letter was followed immediately with advice in February that:[10]

> We have agreed to delay implementing any mortgagee sale until after 1 April 2010. The basis for our agreement was that interest would be paid for January and February at the lower rate. That interest has now been paid and we have arranged for it to be paid out to yourself.
>
> The higher portion of the interest is still outstanding and we will in due course collect those monies for you.

[27] Thereafter, attempts were made to complete (or at least progress) the subdivision in an effort to enhance the value of the property. At no stage did Mr MT advise why he and Mr HB considered it necessary to adopt this approach given the confidence expressed in the first letter of 27 January 2010 that no losses were anticipated should a mortgagee sale be necessary. The assurance in that letter was that there would be prompt action taken to protect the investment by way of a

[9] Letter MT to Trust (27 January 2010).
[10] Letter MT to Trust (24 February 2010).

mortgagee sale if the default was not remedied, and the default had not been remedied.

[28] The default compounded when the principal sum was not repaid on 30 April 2010.

[29] Rule 13 requires that on default, the responsible lawyer must advise contributors of the fact that default had occurred (rule 13.1 and 13.2) and specify the action the responsible lawyer proposes to take (rule 13.3(a)). Mr MT complied with these obligations.

[30] Rule 13.3(b) specifically requires the notice to contributors to "request each investor forthwith to advise the responsible lawyer if the investor does not agree with the action or proposed action specified".

[31] Instead of a request in these terms, the letters to the Trust concluded with the following sentence: "If, however, you have any queries in the meantime, please contact the writer". The Standards Committee considered the invitation for contributors to contact the firm if they had any queries, met the obligations imposed by rule 13.3(b). I do not agree - it is not a request in terms of rule 13.3(b).

[32] In reaching my decision I have considered the content of the letters from the perspective of a contributor. The letters advise of the defaults that had occurred. The lawyers who were administering the loans advised what steps they were taking or intended to take to recover the funds for the contributors. They expressed confidence. They invited the contributors to contact them if they had any queries.

[33] That is not the same as requesting the contributor to advise the lawyers if the contributor does not agree with the action or proposed action. Neither did the letters indicate that the lawyers were obliged to consider the views of contributors.

[34] Rule 13.4 requires the responsible lawyer to take into account instructions or advice of each investor when determining the appropriate action to take. If the responsible lawyer has not actively sought instructions or advice, the question has to be asked as to how they took the views of contributors into account.

[35] In situations such as were encountered in this matter, it would seem that the most appropriate means to seek instructions and/or advice from the contributors would have been to call a meeting of investors. Without knowing whether or not this was practical in the circumstances this cannot be considered to be a requirement, but there does not otherwise seem to have been any attempt by Messrs MT and HB to consult

with the contributors, as opposed to pursuing the course decided on by the finance committee of the nominee company. A meeting of contributors would have enabled a free flow of information and contributors may have been encouraged to make further enquiries. A reasonable interpretation of the underlying message in the correspondence sent to contributors was that the lawyers had decided on a course of action and, apart from an explanation as to what that course of action entailed, there was no option open to contributors to voice opposition or propose a different course of action.

[36] I do not consider that the requirements of rules 13.3 and 13.4 have been met. In *AP v ZG* I took the view that a breach of the rules should, in the majority of cases, result in a finding of unsatisfactory conduct.[11] I remain of that view and consequently consider that the conduct of Messrs MT and HB constitutes unsatisfactory conduct by reason of breaches of rules 13.3 and 13.4 of the Nominee Company Rules.

[37] In *AP v ZG* I noted that "a discretion can clearly be exercised when determining penalty, but breaches should otherwise result in a finding of unsatisfactory conduct (in the present regime) in the majority of cases".[12] That discretion (when determining penalty) may reflect the "mild criticism"[13] that Mr DS considered was an appropriate response.

[38] I refer also to a recent decision, *CM v JD and others.* In that review, I took the view that the directors of a nominee company had full authority to make decisions as to the operation of the company. The important proviso to that principle was that such decisions must be taken in accordance with the requirements of the rules.[14]

[39] Rule 13.3 requires the responsible lawyer to make it clear to contributors that they have an option to disagree with a proposed course of action, and rule 13.4 requires the responsible lawyer to take into account instructions and/or advice from investors. These rules place parameters around the authority of the directors to make decisions where a mortgage is in default. In these circumstances, contributors have not surrendered all authority to the directors. The directors are required to act as far as possible in accordance with the wishes of the contributors and to do so, they must actively seek out what those wishes are. That did not occur in this case.

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[11] *AP v ZG* LCRO 278/2012.
[12] At [64].
[13] Above n 6, at [14.7].
[14] *CM v JD* and others LCRO 6/2013 at [38].

Failing to keep contributors informed

[40] Mr LD complains that [Company A] did not provide complete and accurate disclosure to the Trust of all information relevant to the mortgage. In this regard, he points to the failure to advise the trustees of the existence of the second mortgage which became a source of funds to pay interest on the advance to the nominee company. The second mortgage was registered at the same time as the first mortgage and was in fact registered by [Company A] at the same time.[15]

[41] Knowledge of the existence of the mortgage is therefore imputed to the lawyers even if they were not themselves actually aware of it at the time.

[42] Mr LD says that if he had been aware of the existence of the second mortgage he would not have invested Trust funds in the advance. He argues this was relevant information that should have been disclosed and by not doing so the lawyers have breached rule 7 of the Conduct and Client Care Rules[16] (disclosure and communication of information to clients).

[43] In *CM v JD and others* I addressed the relationship between the Nominee Company Rules and the Conduct and Client Care Rules. I noted that:[17]

> … it is necessary to treat each issue on its facts and determine which of the sets of rules applies. Clearly a lawyer cannot stand accused of unsatisfactory conduct for a breach of the Conduct and Client Care Rules when his or her conduct otherwise complies with the Nominee Company Rules.

[44] In AP v ZG I took the view that the Nominee Company Rules are prescriptive.[18] They prescribe what information has to be provided to a contributor intending to participate in an advance. Rule 7 requires a specific authority to be obtained from a contributor before an investment is made. Rule 8 requires the information specified in Schedule 4 to the Rules to be provided to a contributor before an investment is made in accordance with a specific authority. The drafters of the rules clearly did not consider the existence or otherwise of any prior or subsequent mortgage to be relevant information to be provided.

[45] This is a situation where the Nominee Company Rules clearly dictate what information should be provided. [Company A] complied with the rules and, following the approach in *CM v JD*, there can be no finding of unsatisfactory conduct against

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[15] Letter BL to LCS (3 December 2013) at [39].
[16] Lawyers and Conveyancers Act (Lawyers: Conduct and Client Care) Rules 2008.
[17] Above n 14, at [36].
[18] Above n 11, at [64].

Messrs MT and/or HB for breach of the Conduct and Client Care Rules. In any event, there may even be a view that the existence or otherwise of the second mortgage is not considered to be "relevant" information, given that the drafters of the Nominee Company Rules did not seemingly consider it necessary to require that information to be disclosed.

Penalty

[46] I have reversed the determination of the Standards Committee by finding that the conduct of Messrs MT and HB breached rules 13.3 and 13.4. It remains to consider the appropriate penalty to be imposed in the circumstances.

[47] The letter under cover of which the draft decision was sent to the parties requested comments and/or submissions by no later than 8 April, and in particular, I sought submissions with regard to the level of the fine to be imposed. Both parties responded.

[48] In responding on behalf of the applicants, Mr JK advised that "Mr LD accepts the findings made in the draft decision, and therefore does not intend to make any general comments / submissions regarding the draft decision".[19]

[49] In responding on behalf of Messrs HB and MT, Ms BL confined her comments to the appropriate level of penalty to be imposed.

[50] In the review application, Mr LD seeks that the lawyers should be:

(a) Censured.

(b) Ordered to write to all investors advising investors that the firm still holds the [Guarantor 1 and Guarantor 2] guarantees on behalf of investors from which investor losses may be recoverable; and

(c) ordered to pay compensation to the maximum amount of $25,000.[20]

[51] When considering penalty first and foremost, I refer to my comment at [37] above in noting Mr DS' observation that the breach of rule 13.3 was deserving only of mild criticism. I do not consider that a censure falls within the prescription of a "mild

[19] Letter JK to LCRO (8 April 2016).
[20] Lawyers and Conveyancers Act 2006, s 156(1)(d).

criticism". In support of this I refer to the Court of Appeal decision in *NZLS v B* where the Court said:[21]

> A censure or reprimand, however expressed, is likely to be of particular significance in this context because it will be taken into account in the event of a further complaint against the practitioner in respect of his or her ongoing conduct. We therefore do not see any distinction between a harsh or soft rebuke; a rebuke of a professional person will inevitably be taken seriously.

The Court of Appeal therefore viewed a censure as a significant and serious penalty. That does not equate with a mild criticism and I do not think that a censure is warranted.

[52] Mr LD requests an order that Messrs MT and HB write to the contributors advising that the firm still holds guarantees from the [Guarantor 1 and Guarantor 2] from whom losses may be recoverable. In *CM v JD and others* I referred to the powers of the directors of the nominee company to make decisions as to the operation of the company, and to direct the lawyers as Mr LD requests would be to encroach into those powers. That is not the role of the disciplinary process, and in any event I have some doubts that the jurisdiction to make such an order exists.

[53] I do not consider it appropriate to award compensation to the Trust. Section 156(1)(d) of the Lawyers and Conveyancers Act provides that compensation may be ordered "where it appears to the Standards Committee that any person has suffered loss **by reason of** any act or omission of a practitioner …".

[54] The finding of unsatisfactory conduct relates to a failure to request an investor to advise if they do not agree with the action or proposed course of action set out by the lawyers and to actively seek instructions and or advice from contributors. There are too many imponderables as to what would have occurred had the lawyers made a positive request to contributors as required and sought instruction/advice.

[55] Mr LD is adamant that he would have instructed Messrs MT and HB to proceed immediately with the mortgagee sale and he considers that would likely have been the view of the majority in value of investors. The degree of uncertainty about what the views of the majority in value of investors would have been and what the outcome of a mortgagee sale would have been, means that it cannot be said with any degree of certainty that the losses occasioned by the Trust are directly attributable to the conduct in respect of which the finding of unsatisfactory conduct has been made.

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[21] *NZLS v B* [2013] NZCA 156, [2013] NZAR 970 at [39].

There will not therefore be any order that Messrs MT and HB make payment of any compensation to the Trust.

[56] This Office has frequently adopted the view that the most appropriate penalty to impose following a finding of unsatisfactory conduct for a breach of the rules is a fine. In *Workington v Sheffield,*[22] the LCRO underscored a finding of unsatisfactory conduct for a breach of the rules with a fine of $1,000. I consider in this instance that a somewhat greater fine is justified as the instruction/advice of contributors was not actively sought. This is not the same as depriving the contributors altogether of the opportunity to express their views but goes someway to that position. The maximum fine that may be imposed is $15,000.[23]

[57] However, I must be mindful of the fact that neither the Standards Committee nor Mr DS considered this conduct serious enough to warrant a finding of unsatisfactory conduct. A significant fine would therefore disregard those views.

Submissions for the parties

[58] Mr JK's submissions were brief. He advised that Mr LD considered that a fine of $10,000 should be imposed against each of the lawyers: [24]

> [Mr LD]'s view is that the directors of [Law Firm A]'s nominee company displayed a cavalier approach to their obligations under the Nominee Company Rules, and have continued, throughout the complaints process, to dispute that their actions breached the Rules in any way.

Mr JK advised that Mr LD considered "a fine must be set at a level that deters other practitioners from adopting a similar approach to their obligations under the Rules".

[59] Ms BL's responses were somewhat more detailed.[25] She emphasised that the non-compliance with the rules was "in the nature of an oversight" and "inadvertent." She also made reference to the conclusions of the Standards Committee that "in the important matters, the investors' views had been sought".[26] I have differed from the Standards Committee in this regard, and the submission that this is a factor to be taken into account in determining penalty is contrary to that finding.

[60] Ms BL also notes that Mr LD was not constrained from making his views known, and therefore the effect of the breach was minimised. That submission

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[22] *Workington v Sheffield* LCRO 55/2009 at [68].
[23] Lawyers and Conveyancers Act 2006, s 156(1)(i).
[24] Above n 19.
[25] Quotes are from the letter BL to LCRO (8 April 2016).
[26] Above n 7, at [42].

overlooks Mr LD's opinion, that if the views of contributors had been sought as required, and the lawyers had taken those views into account when determining the course of action, the outcome for the contributors would have been different.[27] The fact that Mr LD felt sufficiently confident to express his (uninvited) views, cannot be seen as a mitigating factor.

[61] Ms BL then refers to two other decisions of this Office. She notes that in *AP v ZG,* the breaches were more numerous and egregious than in this case. I accept that submission. In that review, I came to the view that it was not a "case where a fine or censure is called for",[28] taking note of the fact that the lawyer had not been the subject of complaint in over 40 years of practice. Ms BL advises that similarly, Mr HB has been the subject of two complaints over a 49 year career, both of which were dismissed. Mr MT has not been the subject of complaint in his 27 year career.

[62] I take note here also, that the [Law Firm A] nominee company "has effectively been wound down"[29] with only one mortgage to be concluded. This effectively removes the deterrence value of any fine insofar as Messrs HB and MT are concerned, but, as noted by the LCRO in *Workington v Sheffield* the purpose of a fine is also to "deter other practitioners from failing to pay due regard to their professional obligations".[30]

[63] Ms BL also refers to *ET v VL.*[31] This was a case involving a breach of undertaking in which a fine of $4,000 was imposed. Ms BL notes that the breach of the rules in that instance cannot have been inadvertent,[32] as she contends is the case here. The representation that the breaches were an "oversight" or "inadvertent" discounts the level of care that must be applied to ensure the rules to be followed by the directors of a nominee company. The rules are very clear in their requirements, and are minimal in number. It is not unreasonable to expect that a "responsible lawyer" must be fully conversant with the rules. In investing client funds, there is no room for inadvertence or oversights in ensuring the rules are strictly complied with.

Conclusion

[64] In *AP v ZG* I reached the view that neither a fine nor censure was called for. In that case, the relationship between the contributor and lawyer was of considerable

[27] Mr LD considers that if a mortgagee sale had been conducted at an early stage, the loss by contributors may have been less.
[28] Above n 11, at [75].
[29] Above n 25.
[30] Above n 22, at [65].
[31] *ET v VL* LCRO 190/2010.
[32] The lawyer had been reminded 15 times that he had not fulfilled his undertaking.

significance, as the contributor had previously worked for the lawyer and had acted for her parents. She had placed a marked degree of trust in and reliance on the lawyer, and he had betrayed that trust and reliance. Compensation for personal stress and anxiety was therefore the appropriate outcome for both parties. I do not therefore consider *AP v ZG* to be determinative in fixing on an appropriate level of fine.

[65] This case is in line with cases where rules have been breached, and a response to "mark out the conduct as unacceptable"[33] is required. In *Workington v Sheffield,* the LCRO considered that a starting point "in the absence of other factors"[34] was $1,000. In this case, "other factors" exist, in that the "responsible lawyers" (as referred to in the Nominee Company Rules) must ensure they are fully conversant with the requirements of the rules, and adhere to them. They proceeded with a course of action without seeking the views of the contributors, and could be considered to have deprived contributors of the opportunity provided to them by the rules to participate in the decision making process.

[66] Having weighed up all of the factors I consider a fine of $5,000 to be the appropriate level of fine to impose. As there is no differentiation between the roles played by Mr MT and Mr HB, that fine is divided equally between them.

Costs

[67] This Office incurred significant costs commissioning the report from Mr DS. However, I do not consider it reasonable to visit those costs on Messrs MT and HB as the report was commissioned to assist this Office to progress the review more promptly than otherwise would have been the case. The requirement to complete reviews expeditiously[35] is a statutory requirement and it is not reasonable to recover the costs of assistance required to comply with the statutory requirement from these practitioners.

[68] In the circumstances, the usual costs set out in the Costs Orders Guidelines issued by this Office will be applied.

Decision

Pursuant to s 211(1)(a) of the Lawyers and Conveyancers Act 2006, the determination of the Standards Committee to take no further action on the complaints, is reversed.

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[33] Above n 22.
[34] Above n 22.
[35] Lawyers and Conveyancers Act 2006, s 200.

[69] By virtue of the breaches of rules 13.3 and 13.4 of the Nominee Company Rules and s 12(c) of the Lawyers and Conveyancers Act 2006, the conduct of Messrs MT and HB constitutes unsatisfactory conduct.

[70] Pursuant to s 156(1)(i) of the Act, Messrs MT and HB are each ordered to pay the sum of $2,500 to the New Zealand Law Society by way of a fine.

Costs

[71] Pursuant to s 210 of the Act, Messrs MT and HB are (jointly and severally) ordered to pay the sum of $1,800 to the New Zealand Law Society by way of costs of this review.

Publication

[72] I did not request submissions from the parties on the question of publication as I did not consider that publication of the names of the lawyers was "necessary or desirable in the public interest".[36] That view is reinforced by the advice now received from Ms BL that the nominee company has been wound down, and as to the disciplinary record of the lawyers.

[73] There will therefore be no publication of the names of the lawyers, or any other identifying details of the parties or any other persons, the firm or locations of the security property. However, as this decision includes a number of comments about the administration of nominee companies and the obligations of "responsible lawyers" as that term is defined in the Nominee Company Rules, I direct, pursuant to s 206(4) of the Lawyers and Conveyancers Act 2006, publication of the facts of this decision in anonymised format. The decision will also be published in this format in the usual way, on the website of this Office.

Other directors of the nominee company

[74] As something of a postscript to my decision I feel compelled to address another issue that presents in this review, and that is to consider the responsibilities of the other directors of the nominee company.

[75] Mr JK presented the complaint on behalf of Mr LD and the Trust as "regarding the conduct of [Law Firm A] …".[37] The Standards Officer assigned to the complaint

[36] Lawyers and Conveyancers Act 2006, s 206(4).
[37] Letter JK to LCS (26 September 2013).

made contact with Mr JK and advised him that a complaint could not be processed as being against "[Law Firm A]" as that firm was not an incorporated law firm.

[76] I note from a file note of the discussion with Mr JK[38] that he suggested the complaint could be processed against all of the directors of the nominee company, being the "responsible lawyers" as that term is defined in the Nominee Company Rules. The Standards Officer responded that whilst this was "technically" possible, "Standards Committees will generally focus on the lawyers actually involved in the relevant transaction/file". The complaint therefore progressed against Messrs MT and HB.

[77] Messrs MT and HB instructed [Law Firm B] to respond to the complaint on their behalf. Ms BL[39] advised:[40]

> 3. All partners of the firm at [Law Firm A] are directors of the Nominee Company. Mr HB was appointed a director of the nominee company on 3 April 1991 and Mr MT was appointed on 22 April 2002.
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> 4. The Finance Committee, consisting of three [Law Firm A] partners including Mr MT and HB, manages the nominee companies. At all time relevant to this complaint the Finance Committee was convened by Mr MT. Mr HB was a member of the Finance Committee and has been a member for many years. The Finance Committee met fortnightly and in turn provided a monthly report to the [Law Firm A] partnership.
>
> 5. The Finance Committee would consider loan applications on behalf of the nominee company and complete due diligence in relation to any loans which were being considered. Following that process, and assuming the due diligence process confirmed the appropriateness of the loan, the Finance Committee would approve the loan application and forward an offer to the borrower.

[78] Ms BL did not suggest that Messrs MT and HB denied responsibility, or that responsibility should be spread wider to the other directors of the nominee company. By adopting the approach recorded by the Legal Standards Officer in her file note (focusing on the role of the lawyers actually involved in the transaction) the Lawyers Complaints Service is diluting somewhat the provisions of the Nominee Company Rules. I consider therefore I should take some time in this decision to include a discussion about the Rules, as well as some decisions of this Office and the Lawyers and Conveyancers Disciplinary Tribunal.

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[38] File note taken 9 October 2013.
[39] Correspondence from [Law Firm B] was sent under the joint names of Ms BL and Ms ED, but signed by Ms BL only. I will therefore refer to correspondence from the firm as being from Ms BL.
[40] Above n 2.

[79] I hasten to add at this point, that I do not intend to widen the ambit of this review by formally directing the Standards Committee to reconsider whether or not it should have included all directors of the nominee company in its consideration of Mr LD's complaint. The purpose of this discussion is primarily to act as a warning to lawyers who are directors of nominee companies, that **all directors** have a role, and carry responsibilities, to ensure compliance with the rules and general duties to contributor clients.

[80] It is not necessarily sufficient for a director of a nominee company to surrender control to a limited few, without ensuring there are adequate controls and reporting mechanisms in place, and applying those controls and enforcing reporting mechanisms. Without some measure of responsibility being placed on all directors, the requirement of the rules that all lawyers operating a nominee company are included as responsible lawyers is diluted, or even negatived, thereby reducing the protections for contributors the rules were designed to achieve.

The rules and recent decisions

[81] The terms "responsible lawyer" is defined in rule 3 of the Nominee Company Rules as meaning:

> **responsible lawyer** means every lawyer who operates a lawyers nominee company and includes a lawyer who is, or is required by these rules to be, a director or shareholder of the lawyers nominee company

[82] Rule 4.6 provides:

> 4.6 Each lawyer who operates a lawyers nominee company or who is a principal director or shareholder of a practice which operates a lawyers nominee company must be a director of the company and a majority of the principals or directors of the practice must hold shares in the company.

[83] Rule 6.1 provides:

> 6.1 Each responsible lawyer must take all reasonable steps to ensure that at

> all times the lawyers nominee company complies with these rules, and all obligations imposed upon a lawyers nominee company under these rules are also personal obligations of each responsible lawyer.

[84] The professional responsibilities of directors who are not involved in the administration of a nominee company was addressed in the recent LCDT decision *Auckland Standards Committee v Burcher, Short and MacDonald.*[41]

[85] The three respondents were "senior, respected practitioners, formerly in partnership with each other … ":[42]

> [5] The nominee company was managed on a day to day basis by Mr Burcher, who accepts he must bear the primary responsibility for the defects identified by [the law society inspector]. For this reason he has pleaded guilty to two charges of misconduct relating to the breaches identified by [the law society inspector], and two charges of "*negligence … of such a degree or so frequent as to tend to bring the profession into disrepute*" …
>
> [6] Mr Short also pleaded guilty to charges arising from both reports, but in his case, all four are at the level of "*negligence … of such a degree or so frequent as to tend to bring the profession into disrepute".*
>
> [7] Mr Short had a significantly less involvement in the daily running of the nominee company (which will be discussed later) but accepted, as a partner and director of the nominee company, he must take responsibility for a lack of governance.
>
> [8] Mr Macdonald had almost nothing to do with the nominee company. But, given the non-compliance with the rules that continued after [the report of the inspector] he also accepted that he had fallen short in his obligations as a partner and director of the nominee company to ensure compliance. Accordingly, he pleaded guilty to two charges of "*negligence … of such a degree or so frequent as to tend to bring the profession into disrepute".*

[86] Later in the decision, when discussing relative culpability, the Tribunal made the following comments:

> [38] In terms of relative culpability Mr Burcher plainly accepts the major responsibility in this matter …
>
> [39] For his part Mr Short expresses his acceptance of guilt on the basis of strict liability. However, we do not entirely accept his contention that he was so divorced from the running of the nominee company that he was not able to exercise better governance than was demonstrated.
>
> [40] While we accept that Mr Macdonald was the litigation partner and certainly distant from the running of the nominee company, he too has to accept responsibility as a director of that company, which was managing large sums of money on behalf of others. He failed in his obligation to

[41] *Auckland Standards Committee v Burcher, Short and MacDonald* [2015] NZLCDT 47.
[42] At [1]. All quotes hereafter are from this Tribunal decision and the paragraph number precedes each quotation.

> ensure that the company was being run properly and in accordance with all of its compliance regulations.

[87] The differing levels of culpability were reflected in the penalties imposed by the Tribunal:

- Mr Burcher – censure – nine months suspension - costs $36,000.
- Mr Short – censure – three months suspension - costs $23,000.
- Mr Macdonald – censure – fine $8,000 – costs $6,000.

[88] Name publication was ordered in the case of all three lawyers, the Tribunal noting at:

> [78] … There is simply insufficient evidence to justify a finding that the interests of the practitioners and their families prevail over the interests of the public in the full understanding and openness of disciplinary proceedings.

***AP v ZG* LCRO 278/2012**

[89] The importance of strict compliance with the Nominee Company Rules was touched on by the Tribunal in its decision discussed above. That issue arises in the context of this decision and has previously been considered by me in *AP v ZG.* In that review I made the following comments:

> [63] I do not question [the inspector's] expertise. What I do question is whether this is the right approach to breaches of the Nominee Company Rules, whether major or minor, and whether causative of loss or otherwise. If, as Mr T contends, there is little or no duty of care by a lawyer to contributors to a firm's nominee company, then there is no room to excuse errors or lapses in compliance with the Rules however minor.

[90] The inspector had characterised a number of the breaches of rules in that decision (as in the Tribunal decision in *Burcher*) as technical:

> [64] I consider that Standards Committees should insist on strict compliance with the Rules … I do not consider that there is any room for the exercise of a discretion in determining whether or not the Rules have been breached. A discretion can clearly be exercised when determining penalty, but breaches should otherwise result in a finding of unsatisfactory conduct (in the present regime) in the majority of cases.

[91] I also reached the view that lawyers who put investment proposals before contributors have a duty of care to the contributors. In that regard I noted:

> [54] I am quite satisfied that in putting a lending proposal before contributors, a lawyer cannot disclaim all responsibility for ensuring the proposal is sound. I

> agree that contributors must carry some responsibility for their own decisions. However, I consider that [Mr ZG] had a duty to at least provide the contributors with sufficient information to enable them to make an informed decision and in this regard, I do not think he met his obligations.
>
> …
>
> [57] I do not seek to impose an unreasonable duty of care on a lawyer who puts a proposal before contributors to a nominee company advance, but I do not accept that a lawyer can disclaim all responsibility.

[92] This was the position that had been argued for the practitioner in that case.

[93] The decisions of the Tribunal in the *Burcher* decision, and this Office in *AP v ZG* have some relevance to the present review but, as noted, I do not intend to make any formal referral back directions. Those are matters for the Standards Committee to consider themselves and to exercise their own discretion, or they may be required to address the issues in the event of further complaints being lodged.

DATED this 15th day of April 2016

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O W J Vaughan
Legal Complaints Review Officer

In accordance with s 213 of the Lawyers and Conveyancers Act 2006 copies of this decision are to be provided to:

Mr LD and KL Trust as the Applicants
Mr JK as the Representative for the Applicants
Messrs MT and HB as the Respondents
Ms BL as the Representative for the Respondents
Mr TR as a Related Person
Standards Committee
The New Zealand Law Society