

LCRO 274/2013

**CONCERNING**

an application for review pursuant to section 193 of the Lawyers and Conveyancers Act 2006

**AND**

**CONCERNING**

a determination of the Standards Committee

**BETWEEN**

**AQ**  
Applicant

**AND**

**MR KX and [LAW FIRM X]**  
Respondents

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

**DECISION**

**Introduction**

[1] Ms AQ has applied for a review of a decision by a Standards Committee to take no further action in respect of her complaint concerning the conduct of the respondents, Mr KX and [Law Firm X].

**Background**

[2] Ms AQ's complaint relates to her losing money she paid to the promoter of a proposed residential development known as [Development Complex] at [Area 1].

[3] The development was apparently intended to be carried out in stages. The development company was [Company V] whose sole director was Mr GR. Mr KK acted for [Company V] and allowed its trust account to be used to receive funds on behalf of [Company V], and pay money out on behalf of its client.

[4] Before any construction work began the development was marketed in New Zealand and [Overseas]. The marketing [Overseas] was carried out by [Company Y] and [Company B]. Mr GR was apparently the managing director of [Company Y].

[5] Following a promotion seminar given by Mr GR in [Overseas Country] on 28 May 2011 Ms AQ elected to buy options to purchase five units in stage 2A of the development. Ms AQ signed reservation forms to purchase the five options and paid a deposit for each option. This was part of an investment strategy to assist Ms AQ's application to immigrate to New Zealand.

[6] In her 26 March 2013 email to the Lawyers Complaints Service Ms AQ said she paid a total of \$25,000 to [Company B]. Those funds were apparently forwarded to [Law Firm X]'s trust account, because [Law Firm X] issued a trust account receipt to Ms AQ.

[7] Ms AQ also signed options for a first right of refusal (FRR) to purchase the five units. The FRR agreements recorded that the parties were [Company V] on behalf of the [Trust V] as the FRR issuer, and Ms AQ as the FRR holder.

[8] Clause 1.1 of the FRR agreements defined the FRR price as \$65,000. Clause 2.2 required \$5,000 of this sum to be paid on execution of the agreement and the \$60,000 balance to be paid 10 days after the execution date. The agreements were dated 29 May 2011, although in some cases the 10-day period appears to have been varied.

[9] The exercise by [Company V] was to raise capital to support the development of [Area 1].

[10] The FRR entitled Ms AQ to a refund if her transactions did not reach fruition.

[11] Ms AQ paid money in to [Law Firm X]'s trust account pursuant to the FRR for the benefit of [Company V].

[12] [Law Firm X] issued trust account receipts to Ms AQ. Some of those do not appear to reconcile with Ms AQ's figures.

[13] It is not clear whether [Law Firm X] sent copies of its trust account receipts to Ms AQ, although on 19 July and 30 September 2011 [Company Y] sent five identical letters to Ms AQ, each enclosing a separate receipt.

[14] The receipts were headed “[Development Complex]” and were signed by a [Company V] director. Each one recorded that [Company V] had received \$65,000 from Ms AQ as an option fee in respect of a specific numbered unit.

[15] The [Development Complex] development did not proceed as planned and by November 2012 Ms AQ was pressing for the return of her money. It later transpired that [Law Firm X] had paid all the funds it had received on behalf of [Company V] out, on Mr GR’s instructions, to [Company V] and other parties on its behalf.

[16] [Company V] was placed into liquidation on 8 February 2013. The liquidator’s first report dated 13 February 2013 noted that [Company V]’s failure was attributed to difficulties in obtaining resource consent for the proposed development and problems with management. It also recorded that substantial funds were raised from overseas investors, whose funds had been paid to a number of companies to develop the project.

[17] The report estimated the total owed to unsecured creditors at \$12m and listed Ms AQ as well as [Law Firm X] as unsecured creditors. According to the liquidator’s report dated 20 March 2015 the liquidation is not yet complete but a distribution to unsecured creditors is unlikely.

### **The complaint and the Standards Committee decision**

[18] Ms AQ lodged a complaint with the New Zealand Law Society Complaints Service (NZLS) on 11 March 2013. In subsequent correspondence Ms AQ amplified the complaint and provided further documents.

[19] The substance of Ms AQ’s complaint was that:

- (a) [Law Firm X] was engaged by [Company V] to prepare the FRR agreement and knew that [Company V] did not own the [Area 1] land or have the necessary consent for the proposed development of that land and was aware that the process and documents relating to the FRR agreements were the subject of an intellectual property right asserted by a third party, Mr ED.
- (b) [Law Firm X] paid out the funds which Ms AQ had transferred to its trust account without notifying Ms AQ or seeking her approval. That payment

was concealed from Ms AQ and was not disclosed until November 2012 with the result that she has now lost all of the funds.

- (c) New Zealand-based FRR holders were invited to make their payments into the trust account of another firm of solicitors, [Law Firm C] but overseas FRR holders were required to make their payments into [Law Firm X]'s trust account. There was no reason for treating payments from overseas FRR holders any different than payments from New Zealand-based FRR holders.
- (d) [Law Firm X] should have anticipated or foreseen that the FRR holders such as Ms AQ could be severely affected and may suffer losses if their deposited funds were released from [Law Firm X]'s trust account, and should also have been aware that the trust account may be used as a vehicle for what Ms AQ described as a money scam.

[20] [Law Firm X] was invited to respond to Ms AQ's complaint and did so on 19 March 2013, briefly amplifying that response on 13 June 2013. The substance of [Law Firm X]'s responses was that:

- (a) They acted for [Company V], whose promotion of the [Development Complex] development included the concept of a right of first refusal to purchase units in the development.
- (b) [Company V] asked if [Law Firm X] trust account could be used to receive payments made by purchasers so as to provide a central point for payment and enable a clear record of payments.
- (c) The FRR agreement clearly provided that payments were being made to [Company V] and that those payments were a fee to obtain the first right of refusal to purchase units in the development.
- (d) The FRR payments were not a deposit for the purchase of a property and the FRR made no provision for any payments to [Law Firm X] to be held as a stakeholder or in any other capacity for the purchaser.
- (e) It was clear that the payments to [Law Firm X] were for [Company V] and that in accordance with [Company V]'s instructions [Law Firm X]

subsequently paid funds either to [Company V] or to third parties at [Company V]'s direction.

- (f) [Law Firm X] had no knowledge of any statements made by third parties to Ms AQ that her payments would be held in the trust account and would not be paid out from that account.
- (g) [Law Firm X] denies a failure to forecast or foresee how severe consequences would be to investors, or that the trust account might be used in a financial scam.

[21] The Standards Committee delivered its decision on 2 August 2013.

[22] The Committee determined, pursuant to s 138(1)(f) and 138(2) of the Lawyers and Conveyancers Act 2006 (the Act) that no further action on the complaint was either necessary or appropriate.

[23] In reaching that decision the Committee determined that:

- (a) The FRR agreements were an option for a first right of refusal to acquire units in the development. The agreements stated that the FRR payments were to be made to [Company V] as the FRR issuer in cleared funds to a nominated bank account.
- (b) There was no provision in the FRR agreements that the funds were to be held in trust or that they would not be distributed to [Company V].
- (c) The term "deposit" in the FRR agreements was used in the context of any eventual sale and purchase agreement that may be entered into in relation to the units, where it provided for the contribution of any payment under the FRR agreement towards that deposit.
- (d) [Company V] was [Law Firm X]'s client. Once the payments were received into its trust account [Law Firm X] was obliged to disburse the funds in accordance with [Company V]'s instruction.
- (e) [Law Firm X] did not breach any trust account obligations in relation to Ms AQ.
- (f) There was not sufficient evidence to make a finding that [Law Firm X] had breached obligations in Rules 2.4 and 11.4 of the Lawyers and

Conveyancers Act (Lawyers: Conduct and Client Care) Rules 2008 (the Rules) through their involvement in the preparation of the FRR agreements or their knowledge of the state of affairs relating to the ownership and consent status relating to the development land.

- (g) Ms AQ had already made a complaint to the Serious Fraud Office (SFO) relating to [Law Firm X]'s role in the preparation of the FRR agreements and the development and that complaint was an adequate right of remedy. But if fresh evidence came to light as a result of the SFO's investigation or as a result of any finding by the SFO or any other agency then Ms AQ was able to lodge a further complaint in relation to those matters.

### **Application for review**

[24] Ms AQ lodged an application for review on 11 September 2013. The outcome sought is a direction that the Committee reconsider the whole part of her complaint, reverse its decision and exercise any of the powers that the Committee could have exercised in relation to that complaint.

[25] Ms AQ's application was accompanied by written submissions. These were amplified by her letter dated 23 October 2013. The following is a summary of Ms AQ's submissions:

- (a) Mr [Law Firm X] has acknowledged that [Law Firm X] was involved in preparing the documents used by [Company V] in marketing and selling the FRR agreements, but has sought to downplay the extent and consequences of this involvement.
- (b) An intellectual property claim had been asserted by a third party, Mr ED, in the FRR process and documents. That claim was disputed by Mr GR and [Company V], but it affected or delayed the [Development Complex] development. [Law Firm X] either knew or should have been aware of Mr ED's claim and its effect on the development.
- (c) The [Development Complex] development was devised by or involved a network of related companies, which were either controlled or operated by Mr GR and his associates. [Law Firm X] either acted for those

companies or was aware of the connections between them and their likely effect on the development.

- (d) [Law Firm X] also knew or should have been aware that [Company V] was unable to carry out the development, either because [Company V] never had the necessary consents or because it never owned the [Area 1] land, which was sold twice in the period after Ms AQ signed the FRR agreements. The first sale was in June 2012, to a company controlled by Mr SM for \$5.6m. The second sale was in April 2013, to [Company F], for \$9.56m who were not informed of the funds paid by Ms AQ and other FRR purchasers.
- (e) Due to [Company V]'s known inability to proceed with the development [Law Firm X] knew or ought to have known that the FRR agreements had no value and served no legitimate purpose.
- (f) [Law Firm X]'s involvement in preparing the FRR agreements, allowing its trust account to be used to collect the FRR payments and then sanctioning payments from the funds in its trust account to [Company V] or third parties amounts to dishonest conduct because [Law Firm X] has knowingly facilitated the loss of Ms AQ's and other FRR holder's funds.
- (g) [Law Firm X] should have some responsibility for [Company V]'s actions and representations to the effect that the FRR payments would be protected, and for allowing its trust account to be used as a vehicle to collect funds on behalf of [Company V] and the payment out of those funds which has caused loss to Ms AQ and other FRR holders.

[26] [Law Firm X] and Mr KX were invited to comment on Ms AQ's application. They did so in Mr KX's letter dated 8 October 2013 which relied on their initial response to Ms AQ's complaint but also made the following additional submissions:

- (a) [Law Firm X] did not act for Ms AQ and nor did it provide any advice to her.
- (b) [Law Firm X] only acted for its client, the developer, but cannot be responsible for any information given or representations made to Ms AQ by the developer or any of the marketing companies.

- (c) The FRR agreements made it clear that the FRR payments were to be made to [Law Firm X]'s trust account and the funds paid were for the credit of the developer. This was recorded on the trust receipts.
- (d) Once the funds were received in the trust account [Law Firm X] was obliged to follow its client's instructions as to the use of those funds, including payments from the funds held on trust to its client or other parties at the client's direction. There was no contractual obligation for [Law Firm X] to inform Ms AQ when those payments were made.
- (e) [Law Firm X] was not involved in any of the transfers of the land and nor did it know of Mr SM or of any relationship between him and its client.

### **Review on the papers**

[27] In their letter and email dated respectively 8 and 16 April 2014 [Law Firm X] and Ms AQ agreed to the review being dealt with on the papers. This review has been undertaken on the papers pursuant to s 206(2) of the Act, which allows a Legal Complaints Review Officer (LCRO) to conduct the review on the basis of all the information available if the LCRO considers that the review can be adequately determined in the absence of the parties.

### **The role of the LCRO on review**

[28] The role of the LCRO on review is to reach her own view of the evidence before her. Where the review is of an exercise of discretion, it is appropriate for the LCRO to exercise particular caution before substituting her own judgment for that of the Standards Committee, without good reason.<sup>1</sup>

[29] The LCRO has broad powers to conduct her own investigations, including the power to exercise for that purpose all the powers of a Standards Committee or an investigator, and seek and receive evidence. The statutory power of review is much broader than an appeal, and gives the LCRO discretion as to the approach to be taken on any particular review and the extent of the investigations necessary to conduct that review.

### **Nature and Scope of Review**

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<sup>1</sup> *Deliu v Hong* [2012] NZHC 152, [2012] NZAR 209.

[30] The nature and scope of a review have been discussed by the High Court, which said of the process of review under the Act:<sup>2</sup>

... the power of review conferred upon Review Officers is not appropriately equated with a general appeal. The obligations and powers of the Review Officer as described in the Act create a very particular statutory process.

The Review Officer has broad powers to conduct his or her own investigations including the power to exercise for that purpose all the powers of a Standards Committee or an investigator and seek and receive evidence. These powers extend to “any review” ...

... the power of review is much broader than an appeal. It gives the Review Officer discretion as to the approach to be taken on any particular review as to the extent of the investigations necessary to conduct that review, and therefore clearly contemplates the Review Officer reaching his or her own view on the evidence before her. Nevertheless, as the Guidelines properly recognise, where the review is of the exercise of a discretion, it is appropriate for the Review Officer to exercise some particular caution before substituting his or her own judgment without good reason.

[31] More recently, the High Court has described a review by this Office in the following way:<sup>3</sup>

A review by the LCRO is neither a judicial review nor an appeal. Those seeking a review of a Committee determination are entitled to a review based on the LCRO’s own opinion rather than on deference to the view of the Committee. A review by the LCRO is informal, inquisitorial and robust. It involves the LCRO coming to his or her own view of the fairness of the substance and process of a Committee’s determination.

[32] Given those directions, the approach on this review, based on my own view of the fairness of the substance and process of the Committee’s determination, has been to:

- (a) Consider all of the available material afresh, including the Committee’s decision; and
- (b) Provide an independent opinion based on those materials.

### **Analysis**

[33] Ms AQ’s investment was speculative. She was not [Law Firm X]’s client. In the circumstances, apart from any trust accounting obligations, [Law Firm X] was required, when acting in a professional capacity, to conduct its dealings with Ms AQ with integrity, respect and courtesy, as rule 12 provides.

<sup>2</sup> *Deliu v Hong* [2012] 158, [2012] NZAR 209 at [40]-[41].

<sup>3</sup> *Deliu v Connell* [2016] NZHC 361 [2016] NZAR 475 at [2].

[34] Rule 12.1 also requires a lawyer, normally, informing a person who is unrepresented that the person has a right to take legal advice.

[35] The two trust receipts issued by [Law Firm X] in July and August recorded that the funds received from Ms AQ had been received for the credit of [Company V]. The same information was recorded on the receipts issued by [Company V] in July and September.

[36] The only security Ms AQ was offered was from [Company Y], which under clause 4.4 of the agreement was obliged to provide her with a deed of guarantee within 20 days of the agreement. It is not clear whether those guarantees were provided, but it is apparent that, like all of the other FRR purchases, Ms AQ would have little prospect of recovering her money if the development did not proceed. That is the nature of speculative investment.

[37] The FRR agreements contained no recommendation to seek legal advice before deciding whether to purchase a FRR option.

[38] Nor do the FRR agreements contain any warning about the potential consequences of purchasing the option or an explanation of what [Company V] would or was entitled to do with the FRR payments.

[39] The question is whether by failing to include provisions of that nature, [Law Firm X] contravened rule 12 by failing to conduct professional dealings with integrity, and, as rule 12.1 requires, advising likely signatories that they were entitled to take legal advice independently.

[40] None of the more speculative aspects of the circumstances leading to Ms AQ's complaint relate to a breach of professional standards by [Law Firm X]. There is no evidence that [Law Firm X] was responsible for any failure to obtain consent or purchase land before the scheme proceeded. Although the FRR agreements were used and [Law Firm X] acknowledges its role in drafting and preparing those, it was not [Law Firm X] that used the agreements. There is no evidence that Ms AQ ever had direct interaction with [Law Firm X] before paying money into its trust account.

[41] [Law Firm X]'s obligations were to document their trust account transactions and pay money out in accordance with its clients' instructions. [Law Firm X] says that was the limit of their involvement. The thrust of Ms AQ's application is that [Law Firm X] acknowledged its involvement must be seen in context with other events during the

development, which [Law Firm X] must have been aware of because they acted throughout as [Company V]'s solicitors.

**Did [Law Firm X] allow [Company V] to use its name to appear trustworthy?**

[42] I consider that the Committee correctly identified Rules 2.4 and 11.4 as governing the context in which [Law Firm X]'s conduct must be assessed. I accept that their conduct cannot be divorced from the circumstances in which capital was obtained from overseas parties. However, any failing must be seen in the context of [Law Firm X]'s obligations to its clients. This review process is not a suitable forum in which to determine the allegations Ms AQ makes against [Law Firm X] and [Company V], particularly where, as she says, she made her concerns known to the SFO.

[43] For the following reasons I consider there is insufficient evidence to be satisfied that [Law Firm X]'s conduct fell below appropriate professional standards:

- (a) There was nothing intrinsically or inherently wrong in [Law Firm X]'s involvement or assistance in the preparation and drafting of the documents securing the venture capital borrowing. There is insufficient evidence on which to form the view that when the documents were prepared, [Law Firm X] knew [Company V] might use the documents it had prepared for anything other than a proper purpose, or that [Law Firm X] was aware of the intellectual property claim apparently asserted elsewhere.
- (b) There is no evidence to suggest that [Law Firm X] was involved in the marketing of the [Development Complex] development or any representations made to Ms AQ by [Company V], Mr GR or anyone else.
- (c) The FRR agreements specifically required payments of the price to be made to [Law Firm X]'s trust account. The agreements did not say, nor could they readily be read to have inferred, that those payments would be held on trust for Ms AQ. It is reasonably obvious from the face of the documents that the purpose of the borrowing was to raise capital to enable the development to be completed. It was not Mr KX's obligation to carry out due diligence on his client. He would have been entitled to rely on assertions made by his client, unless he knew them to be false.

This Office is not well placed to inquire into allegations of that nature at first instance.

- (d) The question that arises in relation to professional standards is whether [Law Firm X] issued a receipt recording Ms AQ's payment pursuant to Reg 12(5) of the Lawyers and Conveyancers Act (Trust Account) Relations 2008. The evidence shows compliance with that obligation.
- (e) [Law Firm X] acted for [Company V]. It did not act for Ms AQ, who must be taken to have had the opportunity to seek independent legal advice before electing to proceed with what was plainly a fairly speculative venture.
- (f) There is insufficient evidence to show Mr KX or [Law Firm X] should be held responsible for conduct Ms AQ alleges against its client.
- (g) Once [Law Firm X] received funds into its trust account, it was obliged to follow its client's instructions as to the use of those funds, including making payments at [Company V]'s direction. There is nothing obviously unusual in paying funds out for purposes associated with the development, given that was the purpose for which they were received.
- (h) In the circumstances, I consider there is insufficient evidence on which to conclude that [Law Firm X] assisted or advised [Company V] to engage in fraudulent or criminal conduct in terms of rule 2.4.
- (i) There is also insufficient evidence to form the conclusion that Mr KX or [Law Firm X] were involved in the applications for consent for the development or the subsequent transfers of the development sites. There is insufficient evidence to show that [Law Firm X] was aware of any dubious conduct by its client as alleged by Ms AQ.
- (j) Ms AQ's application is silent on the status of her complaint to the SFO. Although her application does not criticise this part of the Committee's decision, for completeness I consider that the Committee was correct to determine its inquiry on the basis that the SFO complaint and the opportunity to lay a fresh conduct complaint based on the outcome of any investigation provided Ms AQ with an adequate alternate remedy.

**Decision**

Pursuant to s 211(1)(a) of the Lawyers and Conveyancers Act 2006 the decision of the Standards Committee is confirmed.

**DATED** this 17<sup>th</sup> day of May 2016

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**D Thresher**  
**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:

Ms AQ as the Applicant  
Mr KX and [Law Firm X] as the Respondents  
Mr LL as a Related Party  
A Standards Committee  
The New Zealand Law Society