IN THE HIGH COURT OF NEW ZEALAND
TIMARU REGISTRY

CRI 2011-076-1948
[2014] NZHC 2500

THE QUEEN

v

EDWARD ORAL SULLIVAN,
ROBERT ALEXANDER WHITE and
LACHIE JOHN McLEOD

Hearing:	12, 13, 17, 18, 19, 21, 24, 25, 26, 27, 31 March 2014 1, 2, 3, 4, 7, 8, 9, 14, 15, 16, 28, 29, 30 April 2014 1, 2, 5, 6, 7, 8, 9, 13, 14, 15, 22, 26, 27, 28, 29, 30 May 2014 3, 4, 5, 6, 10, 11, 12, 17, 18, 19, 20, 24, 25, 26, 27 and 30 June 2014 21, 23, 24, 28, 30 July 2014 5, 6, 7, 8, 12, 13, 14, 15, 16, 18 August 2014
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Verdicts:	14 October 2014

VERDICTS AND SUMMARY OF REASONS FOR VERDICTS OF HEATH J

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Verdicts

[1] Mr Sullivan, Mr White and Mr McLeod, I will now give verdicts on each charge in the indictment. I will then ask you to be seated. I will then explain, in summary form, why I have entered the verdicts on each charge.

[2] Following some brief observations about trial rulings on which I am lifting suppression orders today, I will deal with consequential issues arising out of my verdicts.

[3] I give the following verdicts:

(a) **Count 1 – false statement by promoter**

Mr Sullivan	Not Guilty
Mr White	Not Guilty

(b) **Count 2 – false statement by promoter**

Mr Sullivan	Guilty

(c) **Count 3 – false statement as promoter**

Mr Sullivan	Guilty

(d) **Count 4 – false statement as promoter**

Mr Sullivan	Guilty
Mr White	Not Guilty

(e) **Count 5 – false statement as promoter**

Mr Sullivan	Guilty

(f) **Count 6 – theft by person in a special relationship**

Mr Sullivan	Not Guilty

(g) **Count 7 – theft by a person in a special relationship**

Mr Sullivan	Not Guilty
Mr White	Not Guilty
Mr McLeod	Not Guilty

(h) **Count 8 – theft by a person in a special relationship**

Mr McLeod	Not Guilty

(i) **Count 9 – obtaining by deception**

Mr Sullivan	Guilty

(j) **Count 10 – obtaining by deception**

Mr Sullivan	Not Guilty
Mr White	Not Guilty
Mr McLeod	Not Guilty

(k) **Count 11 – false accounting**

Mr McLeod	Not Guilty

(l) **Count 12 – false accounting**

Mr McLeod	Not Guilty

[4] Please be seated while I summarise my reasons for returning those verdicts and deal with ancillary issues.

Summary of reasons for verdicts

[5] My full reasons for verdicts are very lengthy and are not capable of being summarised readily. Necessarily, what I say today will be incomplete. There will be differences of expression in what I say today from what is written in my full reasons. No inconsistency is intended. To the extent some might be thought to exist, my full reasons take precedence.

[6] The prepared remarks that I am about to give will be distributed to counsel and media representatives once this part of the hearing concludes. They will also be sent to the same people by email, along with copies of my full reasons for verdicts and the trial rulings to which I shall refer later. These remarks and the full reasons will be posted on the Decisions of Public Interest part of the Courts of New Zealand website as soon as is practicable. The other rulings will go onto the Judicial Decisions On-line site in due course.

[7] While I have pronounced the verdicts in the order in which the charges appear in the indictment, I shall explain my reasons on each charge, in chronological sequence. The remarks I will now make are directed at those who have a working knowledge of the seven transactions to which I shall refer. I acknowledge that some parts of what I say may not be readily understood by those who have not had an opportunity to gain that knowledge.

Background

[8] Messrs Sullivan, White and McLeod were charged with offences involving dishonesty arising out of the way in which South Canterbury Finance Ltd was directed and managed. At material times, Messrs Sullivan and White were directors of the company and Mr McLeod was its Chief Executive Officer.

[9] My task, sitting as a Judge without a jury, was to determine whether the accused were guilty or not guilty on particular charges. I am restricted in doing so to

the way in which the Crown's case was presented, based on the particulars of the charges that were provided to the accused before trial. The reason why I am not entitled to depart from that expression of the case is because it may have been possible for allegations framed in different ways to have been met by evidence that I did not hear.

[10] As counsel made clear in their closing addresses, I am not conducting an inquiry into the collapse of South Canterbury. Nevertheless, I have found it necessary to make a number of findings about the way in which the board and senior management undertook their functions. For example, because I have concluded that the board did not review the content of prospectuses or financial statements to be included in them at their meetings, I have approached questions of knowledge and intent by reference to evidence about what was actually known to an accused at a particular time. I decided that it was unsafe to draw inferences about what ought to have been known to them in circumstances where there was no convincing evidence that collective consideration had been given to relevant issues.

[11] On Mr Hubbard's own figures, prepared at the end of October 2008, South Canterbury needed to raise capital of something in the order of $90 million to survive. The downturn in the property markets and the later systemic financial crisis of 2008 and beyond exposed the fragile capital structure on which South Canterbury had operated and drove the directors to respond to difficult problems in (what I would term) a "knee-jerk" fashion, rather than by the development and application of a coherent strategy. As a result of subsequent events, South Canterbury was put into receivership on 31 August 2010 with a deficit to holders of debt securities in the order of $1.6 billion.

[12] The Crown's case against Messrs Sullivan, White and McLeod was based on the proposition that "the directors and management of South Canterbury ignored or evaded important controls that should have regulated how the company operated", over the whole of the period of the alleged offending. Mr Carruthers QC, for the Crown, submitted that this "approach to the management of the affairs of the company moved beyond the merely cavalier to the dishonest" and "materially contributed to the company's collapse". He added that "the hallmark of the

offending was a series of related party transactions that were purposefully structured to hide high risk lending".

[13] In my view, the Crown's suggestion of (what amounted to) an underlying culture of concealment between 2004 and 2010 does not withstand scrutiny. The conduct of which the Crown complains is more readily explicable by reference to two market phenomena and the way in which South Canterbury was governed and managed.

[14] The Crown based its allegations on seven transactions and three other events. I do not consider that an examination of the seven transactions over a period of a little over five years can provide a safe foundation for an allegation of continuous concealment of information from the public. As an illustration of that point, the first two transactions were entered into in 2004. It is alleged they ought to have been disclosed in Prospectus 55, on offer between 19 November 2004 and 28 October 2005. The next allegations of concealment arose out of alleged material non-disclosures in Prospectus 57, relating to what have been called the Woolpak and Hilltop transactions. They had their origins in events that occurred around March and April 2006. No charges arose out of statements in the intervening offer document, Prospectus 56.

[15] One only needs to read the five prospectuses in issue (Prospectuses 55, 57, 58, 59 and 60) to realise what a small part of South Canterbury's business was represented by the seven transactions.

[16] Rather than a culture of concealment, I have concluded that there were two market phenomena which had a significant impact on the way in which South Canterbury was governed and managed over the period covered by the alleged offending.

[17] The first was a period of rapid growth, between 30 June 2004 and 30 June 2008. During this period, corporate governance and management procedures used by South Canterbury proved inadequate to deal with significant

increases in money received from investors who were subscribing for debt securities on the basis of the three prospectuses in issue, during this time.

[18] In this period, South Canterbury moved from being a company with total assets of about $750 million as at 30 June 2004, to one with almost $2 billion by 30 June 2008. The absence of a robust loan authorisation process and a less than orthodox approach to debt impairment were contributing factors to the problems that South Canterbury faced when a major financial downturn occurred in mid to late 2008.

[19] The corporate governance procedures adopted by South Canterbury during this period (and, indeed, beyond) were more nearly analogous to those of a closely held company than one which solicited funds from the public. That was due to Mr Hubbard's historical influence over the company's affairs. South Canterbury's parent company, Southbury Group Ltd, was owned and controlled by interests associated with Mr Hubbard. Despite attempts from other directors to change his ways, Mr Hubbard was unable or unwilling to grasp the need to adapt the existing governance and management procedures to the contemporary business environment in which South Canterbury was operating. As one witness confirmed, Mr Hubbard regarded related party loans as the safest of all because he had more control over them.

[20] I have mentioned a "less than orthodox" approach to debt impairment. It was common practice for South Canterbury's parent company Southbury to acquire "problem loans" from South Canterbury shortly before balance date. This had the effect of either removing or minimising the need for South Canterbury to provide for impaired debt, as the accounting records showed an injection of new funds by Southbury to replace the non-performing debt. Often, however, moneys advanced by Southbury would be repaid after balance date. As a result, the true state of the inter-company account was not transparently reported to investors. Indirectly, the way in which Southbury acquired "problem" loans operated as a disincentive for South Canterbury to manage non-performing loans rigorously.

[21] There was a special relationship between South Canterbury and Southbury. That manifested itself most clearly in lending arrangements by which Southbury could obtain finance almost at will from South Canterbury. No documents were produced to prove the nature of a facility to Southbury, or the basis on which moneys owed by that company to South Canterbury were secured. However, I cannot exclude the possibility that such documents did exist. There were deficiencies in the investigation by the Serious Fraud Office that could have resulted in documents of that type not being located. On the preponderance of evidence, I am satisfied that the directors and management of South Canterbury acted on the basis that Southbury could draw down to at least 35% of shareholders' funds without prior approval from the board or a credit committee. That percentage was fixed by reference to a single entity exposure provision in the operating debenture trust deed.

[22] The second phenomenon arose from the impact on South Canterbury's fragile business model of a downturn in the property market around mid June 2008, and what became known as the global financial crisis from about September 2008. On 24 July 2008, Mr McLeod was reporting to the board that only three finance companies were doing "limited lending" at that time, one of which was South Canterbury. At the same meeting, Mr McLeod reported that one of the "current challenges" for South Canterbury was "surviving".

[23] When property values fell in mid to late 2008, it had an adverse impact on both Southbury and South Canterbury. Not only did the downturn impact on the value of securities taken for particular loans, but consequential problems for borrowers meant that many were rendered illiquid and were unable to maintain principal and interest payments. The ability for regular inter-company advances to be made from Southbury to South Canterbury was also compromised.

The Guarantee Deed, the bank facilities and debt impairment

[24] Aside from the seven transactions, there are three other issues that require consideration:

(a) The first involved South Canterbury's entry into the Non-Bank Retail Deposit Takers' Scheme established by the Government in October

2008. As a result of acceptance into the scheme, the guarantee given by the Crown was triggered on receivership of South Canterbury meaning that a sum of about $1.58 billion was paid to qualifying investors at that time. Issues arising out of the guarantee are addressed in respect of counts 7 and 10; and

(b) The second concerns allegations of material mis-statements in Prospectus 59 in relation to an undrawn "committed" bank facility of $150 million. This arises in respect of count 4.

(c) The third is an allegation of a deliberate under-statement of the level of impaired debt in Prospectus 60. This arises in respect of count 5.

Count 1: Prospectus 55 – false statement by a promoter

[25] Messrs Sullivan and White were charged with knowingly making materially false statements in Prospectus 55, the prospectus on offer between November 2004 and October 2005, with intent to induce potential investors to subscribe for the debt securities on offer. The alleged false statements relate to transactions involving Shark Wholesalers Ltd. There were two transactions. In the first, known as Shark 1, money had been advanced to enable a relatively orthodox goods warehousing arrangement to be entered into. The second, known as Shark 2, was the provision of funds by South Canterbury to enable Shark Wholesalers to buy shares in another of South Canterbury's related companies. It was accepted that Shark and South Canterbury were related parties for disclosure purposes.

[26] I found both Mr Sullivan and Mr White not guilty on count 1 because:

(a) In respect of the Shark 1 transaction, any non-disclosure was immaterial.

(b) In respect of the Shark 2 transaction, I was not satisfied beyond reasonable doubt that the information the Crown says ought to have been disclosed was material.

Count 9: Woolpak transaction – deceptive conduct

[27] Count 9 of the indictment is next in chronological sequence. The Crown alleges that Mr Sullivan falsely represented to a vendor of shares that the purchaser was unrelated to one of Mr Hubbard's companies, and that the representation was made to induce the seller to part with the shares.

[28] Hellaby Holdings Ltd held shares in Wool Services International Ltd. It had previously sold a parcel to Mr Hubbard's interests. As a result, one of Mr Hubbard's companies, Forresters, held about 40% of the share capital of Wool Services. In March 2006, Hellaby asked Mr Hubbard whether he wanted to exercise an option he had been granted earlier to acquire the 19% of shares that Hellaby wished to sell.

[29] At Mr Hubbard's request, Mr Sullivan acted on this transaction on Mr Hubbard's behalf. The shares were acquired by Woolpak Holdings Ltd. That company had been established by Mr Sullivan. A local businessman, Mr Lund, was installed as a director and was shown as the shareholder in the company. Mr Lund's evidence was that he expected to make a small profit from any difference between the purchase and sales prices of the shares if a prompt takeover bid were made by interests associated with Mr Hubbard.

[30] The Crown asserted that Mr Sullivan deliberately misrepresented to Hellaby that the shares in Wool Services were being acquired by an "unrelated party". Hellaby had asked Mr Sullivan to confirm that Woolpak was an unrelated company before the sale proceeded. There was a concern that if Woolpak was related to a principal shareholder of Wool Services, a sale of the shares to it would infringe the Takeovers Code. On 26 May 2006, Mr Sullivan represented to Mr Houldsworth, of Hellaby, that "the buyer is an unrelated party to any other principal Shareholders".

[31] I was satisfied beyond reasonable doubt that when Mr Sullivan made that representation, he knew that Woolpak was related to Forresters, a principal shareholder of Wool Services. He knew that Mr Hubbard controlled Forresters. Woolpak was being established so that Mr Hubbard could exercise an option to buy shares in Wool Services that had come into existence when the initial shares were

acquired. Both Mr Sullivan and Mr Hubbard had the ability to exercise control or significant influence over Woolpak's affairs.

[32] Mr Lund may have believed he would be the beneficial owner of the shares pending an imminent takeover bid from interests associated with Mr Hubbard. However, the correctness of that underlying premise was not established by the evidence. South Canterbury made a loan of nearly $7 million to Woolpak to enable the shares to be purchased. Interest on that loan was capitalised because Woolpak had no source of income from which it could be paid. Later, South Canterbury gave both Woolpak and Mr Lund an indemnity in respect of any liability to South Canterbury for the loan to Woolpak. They are two of a number of factors that led me to the conclusion that Woolpak was beneficially owned by interests related to Mr Hubbard.

[33] Mr Sullivan was aware of potential problems that could arise from triggering requirements of the Takeovers Code or Stock Exchange Regulations. In my view, he deliberately gave a false assurance to Hellaby to ensure the transaction could be consummated. Mr Sullivan knew the representation was material and made it with intent to induce Hellaby to part with the shares. For those reasons, I found Mr Sullivan guilty on count 9.

Count 6: Theft in a special relationship

[34] Count 6 of the indictment alleges that Mr Sullivan committed the offence of theft in a special relationship when, on or about 1 June 2006, he and Mr Hubbard signed a cheque drawn on South Canterbury's bank account to pay a sum of $25 million for the benefit of Southbury. The Crown alleges that Mr Sullivan deliberately dealt with this money contrary to the requirements of South Canterbury's trust deed.

[35] This $25 million payment to Southbury arose out of the Hilltop transaction. The Hilltop transaction was the start of a series of arrangements through which South Canterbury attempted to recover the balance of a loan it had made to the Hudson Group when Hudson sold the Hyatt Hotel in 2005. The hotel was sold to a

company called Regency Auckland Ltd, of which Messrs Sullivan and McLeod were directors, and Southbury the beneficial owner of its shares.

[36] A series of steps were taken. It was intended that the hotel be sold so that Regency's interest in it did not appear in South Canterbury's books at the end of June 2006. Arrangements were made to sell to interests associated with Mr Neville Mahon. They were entered into in April 2006, with the intention that settlement be effected in late May. That did not prove to be possible.

[37] The payment of $25 million to Southbury was made on 1 June 2006 as part of funding arrangements to enable Mr Mahon's nominee, later named as Hilltop Hotels Ltd, to complete the purchase of the Regency shares. It was used by Southbury to repay a debt to a trading bank. South Canterbury also lent some moneys to Hilltop Hotels to meet refurbishment costs. Because the transaction did not settle as anticipated, Southbury's debt of $25 million remained on South Canterbury's books until 4 December 2008. At that time, a further transaction was undertaken with Quadrant Holdings Ltd. The Quadrant transaction is one to which I return later.

[38] Somewhat counter intuitively, the crime of theft in a special relationship does not involve proof of dishonesty on the part of an accused. For example, for this charge to be proved the Crown must show that Mr Sullivan had control over depositors' funds and deliberately applied that property in contravention of some "requirement" that he knew demanded him to deal with that property in some other way; in this instance the debenture trust deed. It is the knowledge of the requirement and the deliberate application of property contrary to it that provides the mental element of the crime.

[39] A general requirement involving, for example, the way in which the business of a company should be conducted is not sufficient. A specific requirement to do something is necessary. As a matter of law, I have held that specific requirements to deal with property in terms of both the debenture trust deed and the Crown guarantee deed are sufficient to give rise to an offence, if all other elements are proved.

[40] So far as count 6 is concerned, Mr Sullivan's belief about the nature of what I have described as the "special relationship" between South Canterbury and Southbury means that I cannot exclude the reasonable possibility that Mr Sullivan honestly believed he was entitled to sign the cheque for $25 million in favour of Southbury. In particular, I have placed weight on the actual circumstances in which the cheque was drawn, the historical practices that attached to the advancing of funds between those two companies, and the existence of a provision in the trust deed that Mr Sullivan believed enabled Southbury to borrow up to 35% of shareholders' funds. I found Mr Sullivan not guilty on count 6.

Count 11: False accounting

[41] Count 11 also relates to the cheque for $25 million paid by South Canterbury to Southbury. The Crown alleged that, on or about 1 June 2006, Mr McLeod was responsible for creating a physical ledger card in the name of "Hilltop Hotels Ltd". The Crown asserted that the entry of the payment of $25 million on that card was designed to mask the true nature of the advance to Southbury.

[42] There was no evidence that Mr McLeod was generally involved in creating stock ledger cards of this type. Nor was there any documentary evidence to indicate any involvement by him in the creation of the particular card before 26 June 2006.

[43] I accept the Crown's position that someone with knowledge of the transaction must have given the instruction for the card to be established. In my view, there were two possible candidates; Mr Hubbard and Mr McLeod. I could not exclude the reasonable possibility that Mr Hubbard gave the necessary instruction. I found Mr McLeod not guilty on this charge.

Count 2: Prospectus 57 – False statement by a promoter

[44] Mr Sullivan was charged, in count 2, with knowingly making false statements in Prospectus 57 with intent to induce subscription for debt securities. That prospectus was on issue between 29 September 2006 and 15 October 2007. The relevant financial statements were for the year ended 30 June 2006. The Crown

alleged that the Woolpak lending and the $25 million advance to Southbury ought to have been disclosed, both as to amount and nature.

[45] I was satisfied beyond reasonable doubt that the omission of the Woolpak lending was deliberate and material and was knowingly made by Mr Sullivan with intent to induce investment under the prospectus. In dealing earlier with count 9, my focus was on the relationship between Woolpak and Forresters. This charge, count 2, required me to decide whether Woolpak and South Canterbury were related parties. Woolpak was controlled substantively by Mr Sullivan. Either Mr Sullivan or Mr Hubbard could have exercised control or significant influence over Woolpak. In my view, they were related companies, and Mr Sullivan knew that.

[46] Woolpak borrowed about $7 million from South Canterbury in order to buy the shares. While just under $691,000 of the advance had been made by 30 June 2006, it would still have been the third largest related party advance disclosed. Further, the nature of the transaction was such as to require explanation. In my view, the Woolpak lending ought to have been disclosed as a related party advance and identified as a material contract that was not entered into in the ordinary course of business. It was no part of South Canterbury's business to use depositors' funds to lend money on uncommercial terms to a company that had no ability to meet regular interest payments; particularly when it was made to enable interests associated with Mr Hubbard to circumvent the provisions of the Takeovers Code.

[47] As to the $25 million transaction, the amount was in fact disclosed in Note 19 to the financial statements contained in the prospectus. Having regard to the historical business relationship between Southbury and South Canterbury, I cannot exclude the reasonable possibility that Mr Sullivan believed that the transaction was immaterial or in the ordinary course of business.

[48] Although I found that the Crown's allegation in relation to the advance to Southbury had not been proved beyond reasonable doubt, I found Mr Sullivan guilty on count 2 in respect of material non-disclosure of the Woolpak lending.

Count 3: Prospectus 58 – False statement by a promoter

[49] Count 3 alleges that Mr Sullivan knowingly made false statements in Prospectus 58 with intent to induce subscription for debt securities. Prospectus 58 was on issue between 14 October 2007 and 25 October 2008. The relevant financial statements were from 1 July 2008 to 30 June 2007. The Crown focused on omission of the Woolpak lending and the amount of $25 million plus interest accrued that remained owing by Southbury to South Canterbury in respect of the Hilltop transaction.

[50] For the same reasons given in respect of count 2, I found that the Woolpak lending was omitted in circumstances that gave rise to offending of the type alleged. In addition to the amount advanced as at 30 June 2006, the remaining two tranches were advanced to Woolpak on 3 and 31 July 2006 respectively. As at 30 June 2007, with the addition of capitalised interest, the amount owing by Woolpak to South Canterbury, stood at about $7.38 million. By that stage, the prospect that Mr Hubbard would effect a prompt takeover was forlorn. There was no realistic prospect of a margin being available, as Mr Lund may have expected, to provide a small profit for him.

[51] So far as the Hilltop lending was concerned, the Crown accepted that the amount was disclosed as part of a sum of about $52 million owing by Southbury to South Canterbury as at 30 June 2007. As with count 2, I consider there remained a reasonable possibility that Mr Sullivan did not know that the nature of this lending should have been disclosed as material to a potential investor. Thus, I did not find this particular proved beyond reasonable doubt.

[52] On the basis of the material omission of the Woolpak lending, I found Mr Sullivan guilty on count 3.

Count 10: Crown Guarantee – deceptive conduct

[53] Count 10 was the most serious charge in the indictment. Mr Sullivan, Mr White and Mr McLeod were alleged to be complicit in deceiving the Crown into allowing South Canterbury to enter the guarantee scheme in November 2008.

[54] I found each accused not guilty on count 10. I did so on the basis that the Crown had failed to prove beyond reasonable doubt that any misrepresentation that may have been made to the Crown when it was provided with Prospectus 59 induced the Secretary of the Treasury to sign the guarantee deed on 19 November 2008, as opposed to rejecting South Canterbury's application or deferring it for further consideration.

[55] Mr John Whitehead, the Secretary of the Treasury, made the decision to allow South Canterbury to enter the guarantee scheme. He was not called to give evidence. In those circumstances, I was obliged to determine whether the Crown had proved the element of "inducement" beyond reasonable doubt on the basis of relevant documentary evidence and the oral evidence of Mr Park, a Treasury official who was not involved in the decision to allow South Canterbury into the scheme.

[56] In deciding that I could not exclude the reasonable possibility that the Secretary would have signed the guarantee deed that day regardless, I took into account the following factors:

(a) One of the purposes of the scheme was to maintain the confidence of the general body of public depositors. Another was to avoid capital flight to Australia, where a similar guarantee scheme had been introduced a few days earlier. While the financial system was much more reliant upon the position of banks, there remained very few finance companies in which public depositors could invest. South Canterbury was the largest of those at the time of its application to join the scheme.

(b) Maintenance of the confidence of public depositors had to be seen in light of the systemic concerns that arose out of turmoil in world financial markets around the time the guarantee scheme was introduced. The preamble to the guarantee deed stated expressly that the Crown believed that it was "necessary and expedient in the public interest that the Crown" guarantee certain obligations of South Canterbury, given, among other things, the need "to maintain the

confidence of general public depositors in New Zealand financial institutions such as" South Canterbury.

(c) Documents generated by the Reserve Bank and Treasury in the process of considering South Canterbury's application identify "public confidence" as an important consideration.

(d) No application to join the guarantee scheme was refused in the first few months of the scheme on grounds such as creditworthiness or poor business practice.

[57] As a matter of law, a Court is entitled to draw an adverse inference against a party if a witness is not called and evidence of a fact is exclusively within the knowledge of that party. In the absence of evidence from the Secretary, I could not exclude the reasonable possibility that he would have signed the guarantee deed on 19 November 2008, even if the Crown was right about the alleged material omissions. That is why I found Messrs Sullivan, White and McLeod not guilty on count 10.

Count 4: Prospectus 59 – False statement by a promoter

[58] Both Mr Sullivan and Mr White were charged, in count 4, with knowingly making false and material statements in Prospectus 59, on offer between 23 October 2008 and 22 September 2009. The focus was again on the Woolpak and Hyatt lending, as well as the making of an alleged material mis-statement in respect of the "committed" bank facility of $150 million.

[59] I concluded that Mr Sullivan remained culpable in respect of the Woolpak lending. In addition to the factors to which I referred earlier, I placed reliance on Mr Sullivan's failure to correct Mr Hubbard's denial of beneficial ownership of the shares of Woolpak when challenged about that by Messrs Nattrass and White at a board meeting in April 2008.

[60] Mr White was in a different position. At the April 2008 meeting, Mr White had specifically raised the ownership issue and been assured that Mr Hubbard's

interests were not beneficial owners of the shares held by Woolpak. I was not prepared to second guess the impact of the answer given by Mr Hubbard to Mr White.

[61] Mr White must have become aware of the Woolpak transaction in May 2009. He was one of the signatories to the indemnity given to Mr Lund by South Canterbury. Given Mr White's conscientious nature, I found that he must have asked Mr Sullivan why the indemnity was being given. Having regard to what occurred in April 2008, when the point was put directly to Mr Hubbard and Mr Sullivan did not correct his denial, I cannot rule out the reasonable possibility that Mr Sullivan misled Mr White again.

[62] So far as the Hyatt lending was concerned, Mr Hutton (the Group Accountant) gave evidence that the omission of the amount owing by Southbury to South Canterbury (at that stage about $30 million) was his error. He took responsibility for advising both Mr Sullivan and Mr White that it had been disclosed, when it had not. His evidence was not challenged. In those circumstances, I cannot exclude the reasonable possibility that neither Mr Sullivan nor Mr White realised that the nature and amount of the Southbury lending had not been disclosed.

[63] In November 2007, South Canterbury entered into two banking facilities with Bank of New Zealand and Commercial Bank of Australia. One was for one year, in the sum of $50 million. The other was for three years in the sum of $100 million. The $50 million facility was to expire at the end of November 2008. In Prospectus 59, the facilities were described as "committed" and "undrawn". While accepting they were undrawn, the Crown alleged that there was no "committed facility" of $150 million available from 1 December 2008.

[64] As far as the $150 million bank facility was concerned, I found that both Mr Sullivan and Mr White were aware that the one year facility, for $50 million, would expire on 30 November 2008. Despite evidence that the banks would not have permitted a draw down on the $100 million facility in 2009, I was not satisfied beyond reasonable doubt that Messrs Sullivan and White were aware that a facility for $100 million was no longer "committed".

[65] Mr Hutton, who was responsible for preparing the narratives for the prospectuses, gave evidence that he had intended to change the reference to $100 million but omitted to do so. He also gave evidence that it was his responsibility to provide the dollar values to go with that type of statement. There is nothing to suggest that either Mr Sullivan or Mr White was aware of Mr Hutton's error. Mr Nattrass, another director of South Canterbury, gave evidence for the Crown. He said that he did not notice the mistake.

[66] In addition, I found that the Crown had not proved beyond reasonable doubt that a reference to a $100 million facility would have been material to a potential investor. In the context of disclosing the existence of an undrawn "committed" facility of that type, the difference between disclosure of one of $100 million or $150 million might not have made much difference to an investor's decision. Both are large amounts.

[67] I found Mr Sullivan guilty on count 4 in relation to omission of the Woolpak lending. I found Mr White not guilty on count 4.

Count 7: Theft in a special relationship

[68] Count 7 of the indictment alleges that Mr Sullivan, Mr White and Mr McLeod committed the crime of theft by a person in a special relationship arising out of an alleged advance of just over $39 million made by South Canterbury to Quadrant Holdings on 1 May 2009, as recorded in a loan agreement dated 4 May 2009. The loan is said to have been made contrary to the requirements of the guarantee deed. It is accepted that Quadrant Holdings and South Canterbury were related parties.

[69] The Quadrant transaction followed settlement of the litigation commenced by interests associated with Hilltop Hotels on 4 December 2008. It involved reacquisition of the shares in Regency by Quadrant Holdings from the Mahon interests. This meant that Quadrant Holdings needed to take over debts recorded in South Canterbury's books as being owed by Hilltop Hotels. A debt in Hilltop Hotels' name of around $39 million was replaced by a loan to Quadrant Holdings made on 1 May 2009.

[70] The advances were intended to restructure loans made as part of the Hilltop transaction. However, I rejected a submission that the loans were assumed by Quadrant Holdings, as a matter of law, on the amalgamation of Hilltop Hotels and Quadrant Holdings on 22 April 2009. In my view, the loan of $39 million should be treated as a separate advance which triggered the need to comply with the 1% limit in the guarantee deed.

[71] Quadrant Holdings was established to be the "end owner" of the Hyatt Hotel. Quadrant Holdings and South Canterbury were related parties. Mr Sullivan's brother in law, Mr Symes, was inserted as a director and shareholder of Quadrant Holdings on its incorporation in early December 2008 to distance South Canterbury from that company. Mr Symes had been used in a similar capacity when the Shark transactions were implemented. He had been appointed as a director of Shark Wholesalers Ltd.

[72] In a letter to Mr Symes of 4 December 2008, Mr Sullivan stated, among other things, that South Canterbury wanted to appoint Mr Symes because neither it nor Southbury wished to be the direct owner of the Hyatt. Mr Sullivan made it clear to Mr Symes that all management and other functions would be exercised by himself and Mr McLeod.

[73] All three accused knew of the requirement in the guarantee deed that lending to a single entity could not exceed 1% of shareholders' funds without the written permission of the Crown. Any advance of $39 million to Quadrant Holdings in May 2009 would have breached that requirement. No permission was sought or obtained.

[74] Settlement of the Hilltop transaction was agreed in principle at a board meeting held on 14 November 2008. That was five days before the Crown guarantee deed was signed, on 19 November 2008. By that time, the directors of South Canterbury and Mr McLeod knew both that a "South Canterbury" company would need to acquire the hotel and that the guarantee deed in its final form would contain the prohibition on lending in excess of 1% without permission of the Crown.

[75] The decision to advance $39 million to Quadrant was taken around the time settlement with the Hilltop interests was effected, in December 2008. It was intended that the debt recorded as owing by Hilltop Hotels would be extinguished and the same amount advanced to Quadrant Holdings. There was never intended to be any additional outflow of funds from South Canterbury.

[76] Mr Sullivan and Mr McLeod were delegated with the task of implementing the Hilltop settlement. Although he was party to signing an indemnity in favour of Mr Symes on 17 April 2009, Mr White does not appear to have played any active role in the implementation of the Quadrant transaction from 4 December 2008. I was not satisfied beyond reasonable doubt that Mr White committed the offence of theft in a special relationship in respect of this transaction.

[77] So far as Messrs Sullivan and McLeod are concerned, I have no doubt that they were on notice of circumstances that may have required them to check whether the 1% limit would be breached. However, the level of knowledge that they held was not sufficient, in my view, to make them criminally liable. There is no evidence that they turned their mind expressly to the question whether a loan of the type made would breach the guarantee deed. It is reasonably possible that they honestly believed that in a circumstance where there was no outflow of funds, no permission was required.

[78] I found all three accused not guilty on count 7.

Count 8: Theft in a special relationship

[79] Mr McLeod is charged under count 8 with theft in a special relationship arising out of the Dairy Holdings transaction.

[80] In June 2009, it became clear that South Canterbury was in danger of breaching trust deed covenants involving single entity exposures. Around that time, a related party, Dairy Holdings Ltd, was seeking a loan facility from South Canterbury. South Canterbury was unable to advance further money to Dairy Holdings without breaching the trust deed. A separate arrangement was put into place whereby South Canterbury loaned $12 million to Mr Armer, a director and

shareholder of Dairy Holdings. The Crown alleged that Mr Armer was no more than a conduit and that, in reality, the loan was made to Dairy Holdings, and ought to have been disclosed as such.

[81] In my view, South Canterbury entered into a legitimate transaction with Mr Armer that ensured it did not breach the trust deed. That there was no artifice about the transaction is demonstrated by the fact that, when the receivers of South Canterbury took steps to recover the debt, Mr Armer personally paid $3 million to them to discharge his liability. There was no related party transaction to disclose.

[82] I found Mr McLeod not guilty on count 8.

Count 12: False accounting

[83] Count 12 of the indictment alleges that Mr McLeod, on or about 20 July 2009, caused a false entry to be made in the Great Plains accounting system used by South Canterbury to record a fictitious transaction involving Kelt Finance Ltd, Southbury and South Canterbury.

[84] Kelt Finance was a company in which South Canterbury had a 75% interest. In order to avoid advances to Southbury exceeding 35% of shareholders' funds as at 30 June 2009, a "transaction" was recorded in South Canterbury's books which purported to:

(a) increase a debt owed to South Canterbury by Kelt Finance by $10 million;

(b) record an "advance" by Kelt Finance to Southbury in the sum of $10 million; and

(c) enable Southbury to "use" that $10 million to repay South Canterbury that amount.

That had the effect of bringing the amount advanced by South Canterbury to Southbury below the 35% threshold as at balance date, 30 June 2009.

[85] Mr Brown, the Chief Financial Officer, gave evidence that the Kelt transaction was his brainchild and that he was responsible for its implementation. He said he honestly believed that the transaction was legitimate because it complied with accounting standards.

[86] I am satisfied that Mr McLeod was not involved in the creation of the entries that gave effect to this arrangement. The evidence given by both Mr Brown and Mr Hutton support that view. The entries were made on 20 July 2009 and backdated, in effect, to 30 June 2009. Mr McLeod's first email was to Mr Brown on 24 July 2009. I consider that email was more likely to have been requested by Mr Brown to confirm approval from the board to carry out the entries rather than any instruction from Mr McLeod for them to be done. That is more consistent with the fact that the entries were made on 20 July 2009.

[87] I found Mr McLeod not guilty on count 12.

Count 5: Prospectus 60 – False statement by a promoter

[88] Prospectus 60 was issued on 19 October 2009. By that time, Mr White and Mr Nattrass had resigned as directors of South Canterbury. Mr Sullivan and Mr Hubbard were the directors who made statements in Prospectus 60.

[89] Count 5 alleges that Mr Sullivan made materially false statements in Prospectus 60 with intent to induce persons to subscribe for debt securities offered in that document. The Crown relies on four transactions to establish material omissions, mis-statements involving the absence of other material contracts or matters, the absence of any statements that particular transactions were not undertaken in the ordinary course of business and a deliberate understatement of debt impairment.

[90] I was satisfied that Mr Sullivan was guilty on count 5, based on the allegations made in respect of the Woolpak, Quadrant and Kelt transactions. In particular:

(a) Mr Sullivan was aware that, despite payments totalling just over $3 million made by a Hubbard company, Plum Duff Ltd, the Woolpak debt remained outstanding. As at 30 June 2009, that debt was for more than $6 million. As with counts 2 to 4 that amount and the nature of the loan should have been disclosed, but were not.

(b) Quadrant Holdings was a related party. No reference was made to its indebtedness to South Canterbury which, as at 30 June 2009 was around $40 million. Mr Sullivan was instrumental in arranging this transaction. The Quadrant transaction was not entered into in the ordinary course of business. While South Canterbury's business was to lend money, this was an advance to a related party that was designed to give South Canterbury control over the sale of the Hyatt Hotel. It was no part of South Canterbury's business to own or operate hotels.

(c) The Kelt transaction was a fiction. Mr Sullivan knew that it had been processed in an endeavour to avoid disclosing a breach of the trust deed in relation to related party lending to Southbury. In my view, the word "transaction" is inapt to describe what happened. No money changed hands. No business was transacted. No loan agreement was executed by any of the three parties on or before 30 June 2009. The accounting treatment was no more than window dressing at the cut-off date. I found this particular proved beyond reasonable doubt.

[91] Two further allegations remain:

(a) I am satisfied that the Dairy Holdings transaction was legitimate and could not give rise to an offence in respect of Prospectus 60.

(b) The Crown alleges that Mr Sullivan deliberately understated the amount of debt impairment as at 30 June 2009. In the financial statements for the year ended 30 June 2009, the amount shown for debt impairment was about $77.9 million. By 31 December 2009 that

> allowance had increased to about $244.2 million, an increase of approximately $166.3 million. On balance, I cannot exclude the reasonable possibility that Mr Sullivan honestly believed the impairment disclosed was at the very lowest end of a reasonable range of views on impairment disclosure.

[92] For reasons given in respect of the Woolpak, Quadrant and Kelt transactions I found Mr Sullivan guilty on count 5.

Suppressed trial judgments

[93] During the course of the trial, I was required to give a number of judgments, some of which were suppressed. Two topics required my attention over a number of days, thereby requiring evidence to be delayed. One concerned disclosure of documents by the Crown. They arose in May 2014. Judgments on those topics have already been released. The other involved an application to invoke what is called the co-conspirators' rule of evidence.[1] That, and the problems that flowed from it, happened in June.

[94] The term "co-conspirators' rule" is somewhat of a misnomer. In the circumstances of this case, it was directed to an alleged joint criminal enterprise in which the three accused were all said to have participated. The rule, if applied, enables statements made in the absence of one accused to be used against him provided they are made by co-participants in the joint enterprise and are in furtherance of it. In such circumstances, the accused can be faced with evidence that he cannot contest directly; for example, because he was not present when something was said or done; or not involved as a sender or recipient of correspondence between co-participants.

[95] The judgments that will be released shortly were given on 11, 17 June and 30 June 2014. The rulings arose out of an allegation made by the Crown, in the context of its argument on the application of the co-conspirators' rule, that Mr Brown should be regarded as an unindicted joint participant in a criminal enterprise. That

[1] *R v Sullivan (11)* [2014] NZHC 1312, *R v Sullivan (13)* [2014] NZHC 1359, *R v Sullivan (13) [Reasons]* [2014] NZHC 1365 and *R v Sullivan (15)* [2014] NZHC 1496.

submission was made notwithstanding the fact that Mr Brown had initially been charged in relation to the Kelt transaction but the indictment had subsequently been amended to remove him from criminal prosecution. For all practical purposes, the charge against Mr Brown had been withdrawn. After the Crown raised that issue, I learnt that counsel for the accused intended to call Mr Brown as a witness. Not long after that, the Crown elected not to pursue application of the co-conspirators' rule.

[96] Unsurprisingly, all of this caused problems for the accused. Application was made to the Solicitor-General to have Mr Brown granted immunity from prosecution. That was not granted. At the same time, I heard legal argument on how to remedy the position without infringing the accused's fair trial rights or putting Mr Brown in jeopardy of further prosecution. To deal with the issue, I allowed Mr Brown to have his own counsel, Mr Raymond, present while he gave evidence, so that any potential areas in which he might be asked a question that could put him in jeopardy of criminal prosecution could be drawn to my attention and any appropriate self-incrimination warning given. I was conscious that I might not be able to identify areas of potential jeopardy as quickly as might be necessary.

[97] I made orders suppressing the allegation made against Mr Brown, the legal arguments that were advanced and the presence of Mr Brown's counsel in Court while he gave evidence. Those orders, and those in relation to the judgments that will shortly be released, are now discharged.

[98] I do not consider Mr Brown to have participated in any joint criminal enterprise. He should be regarded as having been absolved from such an allegation. Generally, I accepted his evidence, though in some respects (particularly in relation to the Kelt transaction and the "committed" banking facilities) I detected an element of reconstruction of evidence that tended to portray his actions more benevolently than when viewed objectively in light of contemporary evidence. Having said that, I found Mr Brown to be an honest witness.

Consequential issues

[99] I ask the accused to stand.

[100] Mr Sullivan, I have found you guilty on counts 2, 3, 4, 5 and 9 of the indictment. On those you are convicted. I have found you not guilty on counts 1, 6, 7 and 10 of the indictment. On those you are discharged.

[101] Mr White, I have found you not guilty on counts 1, 4, 7 and 10 of the indictment. On all of those you are discharged.

[102] Mr McLeod, I have found you not guilty on counts 7, 8, 10, 11 and 12 of the indictment. On those charges you are discharged.

[103] Mr White and Mr McLeod, you are each free to go.

[104] I will now deal separately with consequential issues in relation to Mr Sullivan's sentencing.

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P R Heath J