



Receivers' Six Monthly Report on the State of Affairs of
Capital + Merchant Finance Limited (In Receivership)
For the six month period from 24 November 2008 to 23 May 2009
Pursuant to Section 24 of the Receiverships Act 1993
Company Number 1180423

July 2009



31 July 2009

Registrar of Companies
Companies Office
Private Bag 92061
Auckland Mail Centre
Auckland

Capital + Merchant Finance Limited (In Receivership)

Attached is our six monthly report in relation to Capital + Merchant Finance Limited (In Receivership) pursuant to Section 24 of the Receiverships Act 1993. A copy of this report has been sent to Fortress Credit Corporation (Australia) II Pty Limited and Perpetual Trust Limited.

A handwritten signature in blue ink, appearing to read "R G Simpson".

R G Simpson
Receiver

A handwritten signature in blue ink, appearing to read "T W Downes".

T W Downes
Receiver

Contents

Contents

Introduction	1
Particulars of Assets and Disposals of Receivership	
Property	2
Particulars of Debts and Liabilities Outstanding	8
Receipts and Payments	10
Investigations	11

Appendices

Appendix 1 - Restrictions
Appendix 2 - Directory

Introduction

We, Richard Grant Simpson and Timothy Wilson Downes of Grant Thornton were appointed jointly and severally as receivers and managers of all the assets, property and undertakings of Capital + Merchant Finance Limited (“Capital + Merchant Finance” or “the Company”) on 23 November 2007 by Fortress Credit Corporation (Australia) II Pty Limited (“Fortress”).

We were appointed under the powers contained within a general security agreement dated 5 October 2006 issued by the Company.

We set out below our six monthly report on the state of the affairs of the Company as required by section 24 of the Receiverships Act 1993.

Grant Graham and Brendan Gibson of Korda Mentha (“the Second Receivers”) were appointed receivers on 29 November 2007 by Perpetual Trust Limited (“Perpetual”), under its second ranking security over the Company’s assets. Perpetual acts as trustee for some 7,000 debenture holders.

While we have been appointed by the first ranking secured creditor, Fortress, we have been mindful of the need to ensure that all our actions and transactions entered into during our receivership are in the best interests of all of the Company’s stakeholders, including the debenture holders.

The property in receivership comprises all of the assets, property and undertakings of the Company, which are now under our control. At the time of our appointment, the assets primarily consisted of the following:

- Loans advanced to third parties;
- Advances to related parties;
- Accounts receivable;
- Investment in a subsidiary;
- Prepayments; and
- Recorded taxation assets.

The directors of Capital + Merchant Finance at the date of our appointment were:

Neal Nicholls
Owen Tallentire
Colin Ryan
Robert Sutherland

Wayne Douglas resigned as a Director on 15 February 2007.

Particulars of Assets and Disposals of Receivership Property

The table below summarises the reported assets of Capital + Merchant Finance as at 23 November 2007, based on unaudited management information.

Capital + Merchant Finance Limited Draft Management Accounts Unaudited	As at 23 November 2007 \$000's
Cash at Bank	337
GST Refund	173
Accounts Receivable	1,997
Loans and Advances	182,597
Accrued Interest	1,364
Other Investments	4,996
Subsidiaries	8,290
Total Assets	199,754

Loans and Advances

The Company's major asset was the loans and advances, which consisted of 55 loans with a total book value of \$182.6 million.

The majority of the loans were for property development projects in various stages of completion. Interest was accruing and capitalised on most of the loan balances.

The table to the right summarises the priority position of the loans, including the number with first, second or third ranking mortgages, or other securities, along with our realisations to date.

Loan Book	As at 23 Nov 2007 \$000's	Realised To date \$000's
1st Mortgage	1,487	104
2nd/3rd Mortgage	42,269	36,945
Business Loans	13,761	9,760
Related Party Loans & Subsidiary	41,581	18,714
DMT	18,474	121
CMI	65,026	-
Total	182,597	65,644
Paid or Payable to Prior Ranking Securities		41,616
Total Recoveries to Capital + Merchant Finance		24,028

Realisations of all but one of the loans existing as at the date of receivership have now been completed. In the case of a small number of loans, we are continuing our efforts to recover monies under the Lloyds insurance policy, as well as pursuing loan guarantees where possible. With most of the loans, Capital + Merchant Finance was not the first ranking security holder in the assets over which the loans are secured.

From the 55 Loans, gross recoveries of approximately \$65.6 million had been realised as at 23 May 2009. Of this, \$24 million (excluding collection costs) has been recovered by Capital + Merchant Finance, the balance having been paid to prior ranking security holders.

Recovery Strategy

Each loan was individually analysed by us to determine the appropriate strategy for maximising realisations. Due to commercial and confidentiality reasons we are unable to provide specific details in respect of individual loans.

We engaged a range of consultants, legal advisers and valuers to assist in the assessment of respective realisation options.

The options considered for each loan included, but were not limited to:

- Refinancing by the borrower
- Consideration of purchase and/or settlement proposals received
- Partial/full completion of developments with the assistance of the borrower and other financiers
- Formal recovery action through the rights attached to securities held
- An orderly sell down by the borrower, and
- Any other options that may have improved the realisable value of securities held.

Difficulties we encountered with managing the recoveries included:

- Poor quality lending by Capital + Merchant Finance

- Unavailability of credit due to the decline in the property finance sector
- A slowing in the property market
- Decreases in values of assets subject to Capital + Merchant Finance's security.

Mortgages

We have been working in conjunction with prior ranking security holders in formulating strategies to maximise recoveries.

We have achieved total recoveries of \$37 million, of which \$27.2 million was due to prior ranking security holders.

Business Loans

Of the eight business loans totalling \$13.8 million at the date of appointment, one borrower was in receivership and another was in liquidation. Thus, no recovery has been achieved of the \$3.4 million owing by these two borrowers.

We received full recovery from three loans and part recovery on three further loans with the balance of these loans written off. In addition, we received full recovery of a further loan of \$1.6m, which had not been included in the outstanding balance at the date of receivership, as it had been assigned to related parties. Following negotiations with all parties this loan was recovered in full.

Including the \$1.6 million referred to above, total recoveries of \$9.8 million have been received as at 24 May 2009, of which \$4million was due to prior ranking security holders. No further recoveries are anticipated.

Related Party Loans

There were six recorded related party loans totalling \$37.6 million, as at the date of our appointment. The borrowing companies in respect of these loans were controlled by either Messrs Tallentire, or Douglas, or Nicholls.

We have made demand on all of the related parties for the amounts due and placed one into Receivership. We have received full payment from one related party.

Liquidators have now been appointed to Ultratone Holdings Limited and to Capital + Merchant Group Limited. One of the companies from which two of the related party loans were owed is now in liquidation.

In the course of our investigations we identified a number of other loans totalling \$41.1 million that in our view, contain certain “related party” elements, but were not recorded as “related party” loans in the company records. Total recoveries from these other “related party” loans amount to \$1.75 million with the balance required to be written off. The unrecorded “related party” loans of \$41.1 million combined with the recorded related party loans of \$41.58 million amount to some 43% of the total Capital + Merchant Finance loan portfolio. Various matters in relation to these loans have been highlighted to the relevant authorities and are currently under investigation.

Due from Subsidiary

Capital + Merchant Finance was owed \$3.9 million by Numeria Leasing Limited, a subsidiary of the Company. The business and the assets of Numeria Leasing Limited were sold and we received \$2.7

million in repayment of the loan. For further details please refer to the sale process as detailed later in this report.

The company is currently in liquidation and we are pursuing a debt guaranteed by a former Capital + Merchant Finance director.

Diversified Mortgage Trust (“DMT”)

DMT loans of \$18.5 million relate to Capital + Merchant Finance’s participatory interests in loans partially sold to DMT from May 2006 onwards.

Perpetual holds mortgages over security in trust for DMT and Capital + Merchant Finance. Capital + Merchant Finance holds a security position secondary to DMT in these loans.

As Capital + Merchant Finance holds a secondary security position to DMT, realisation of the loans will be dependant on the respective realisations by DMT.

We have been involved in the loan realisation process, where applicable, with DMT on all the loans. To date we have received \$121k from loans with DMT. We estimate further recoveries of \$nil. Any proceeds recovered from these loans will be paid to prior ranking security holders. We are currently working with DMT in an effort to recover losses under the Lloyds insurance policy.

Capital + Merchant Investments Limited (“CMI”)

We were also appointed receivers of CMI by Fortress on 23 November 2007. Fortress has a first GSA charge over the assets of CMI.

Capital + Merchant Finance holds security secondary to CMI on 16 loans. This means that Capital + Merchant Finance will only receive money from CMI when CMI has repaid its debt of around \$50 million owing to Fortress.

To date CMI has recovered \$43.8 million from these 16 loans, of which \$40.2 million has been paid to Fortress as a reduction of the debt. A further \$0.8 million has been advanced by CMI to enable completion of specific property developments.

Based on our review of the CMI loan portfolio, the deteriorating property finance sector and the “credit crunch”, recovery of any funds for Capital + Merchant Finance from CMI is not likely.

Insurance Policies Held

As at the date of receivership, Capital + Merchant Finance held an insurance policy in respect of 42 loans, covering amounts of unrecovered principal.

Due to the substantial affect on the likely recovery, particularly to debenture holders, we have carefully investigated the insurance position.

We have taken legal and specialist insurance advice on this matter and confirm that of the 42 loans, the 16 included with CMI are not covered by the insurance policy.

We are hopeful that there may be coverage in relation to the 15 loans included with DMT.

The remaining 11 loans are still being reviewed to confirm adherence by Capital + Merchant Finance for disclosure and other requirements of the insurance policy.

The insurance policy covers a percentage of unrecovered principal, up to a maximum for each loan of \$3.5 million, with an overall maximum claimable within a twelve month period of \$20 million.

In pursuing this matter with the underwriter, we are experiencing difficulty with a number of loans where technical policy requirements were not adhered to, prior to the date of receivership and this may further invalidate the insurance position. However, we are continuing to pursue this matter and cannot reliably estimate expected recoveries (if any) at this time.

We have requested a refund from the brokers of the premiums paid in relation to the loans included with CMI.

Cash at Bank

The cash at bank held by the Company’s banker has been collected.

GST Refund

Capital + Merchant Finance’s accounts showed a GST refund due of \$173k as at 23 November 2007.

We have reviewed the GST account and returns and a refund of only \$30k is available, which we have recovered. During the course of the

receivership we have continued to file GST returns and to date have obtained refunds totalling \$242k, which includes the \$30k referred to above.

Accounts Receivable

Accounts receivable were represented by trade receivables (\$257k) and prepayments and accruals (\$1.740m). Trade receivables consisted of loan establishment fees, which have been included in the loan recoveries. Prepayments and accruals consist primarily of standard accounting entries to spread expenses already paid over the life of the investments or period of use.

No recoveries are anticipated.

Accrued Interest

This is interest accrued on loans and advances as at the date of the receivership.

Accrued interest has been recovered on loans where full recovery has been obtained. No further recoveries are anticipated.

Other Investments

Other investments include \$4.7 million invested in DMT A, B and C capital notes totalling \$3.2 million and a \$1.5 million security deposit.

The notes and the security deposit were repayable on 31 December 2008, which was delayed until 31 March 2009. Currently portions of class A and B notes have been paid, with full recovery dependent on DMT successfully claiming insurance on defaulted loans.

CMF's C notes rank behind the A and B notes, and these will only be paid out after the full redemption of A and B notes. DMT have indicated recoveries on these are unlikely.

To date we have received \$554k in interest payments.

Investment in Subsidiary

This investment is 100 percent of the shares in Numeria Leasing Limited, which were purchased from Numeria Finance Limited in March 2007.

We removed the Directors of Numeria Leasing Limited and appointed ourselves as Directors.

We offered the business and/or shares for sale via an international tender. We had replies from sixty interested parties and received 16 indicative bids from parties, 4 of which were for amounts sufficient to qualify for due diligence.

We sold the business and assets, fully repaid the first mortgagee, ANZ National Bank leaving \$2.7 million as a recovery for the outstanding loan due to CMF.

There was no recovery on the \$8.3 million investment in the shares of Numeria Leasing Limited.

Taxation

Capital + Merchant Finance's accounts show a tax liability of \$196k as at 23 November 2007.

This figure includes deferred tax liabilities, which when removed for the preparation of the 2007 tax return results in a tax asset of \$219k.

However, any tax claim is limited to the amount available in the Imputation Credit Account. After taking into account the dividends paid to Capital + Merchant Group Limited during the period 1 April 2007 to 23 November 2007 the imputation account and in turn the tax refund is reduced by \$172k.

After liaising with Inland Revenue, we achieved a refund of \$30k.

Particulars of Debts and Liabilities Outstanding

Fortress

Fortress is secured by a General Security Agreement dated 5 October 2006 and a Deed of Priority between Capital + Merchant Finance, Perpetual Trust Limited and Fortress dated 5 October 2006.

To date we have repaid Fortress \$20.9 million. Fortress is owed a further \$2.5 million, including accrued interest, as at 23 May 2009.

Based upon the information available, we expect Fortress will be repaid in full.

Debenture Holders

Debentures comprise:

- Capital Secured Debentures \$90.7 million
- Investment Debentures \$76.3 million

The Capital Secured Debentures are subject to the insurance arrangements referred to earlier in this report.

In addition debenture holders are secured by a Debenture Trust Deed in favour of Perpetual dated 5 April 2002 and amended by a Deed of Modification dated 25 November 2002 and a Deed of Variation dated 19 May 2006. The Trust Deed provides a first ranking security (subject to a Deed of Priority to Fortress) to

Perpetual as trustee representing the interests of all the secured debenture investors.

The secured debenture investors balance consists of approximately 7,000 individual investors.

Estimated Return to Debenture Holders

Our initial estimate was that debenture holders may recover between 14% and 59% of their investment over time. This preliminary estimated range reflected considerable risks and uncertainties relating to the recoverability of certain loans.

Unfortunately the loan quality, the deteriorating property market and lack of alternative credit to facilitate refinancing options have had an adverse effect on our ability to recover outstanding loans and assets.

As a consequence we revised our estimate of recoveries to debenture holders to a recovery of up to 2% of their investment, prior to interest accrued on the first chargeholders debt and receivership costs. After accrued interest and receivership costs we expect recoveries to be \$nil for debenture holders from the assets of the company. In our view, the only recoveries for debenture holders will be from insurance claims and any legal claims against various parties.

We detail our revised estimate below:

Capital + Merchant Finance Estimated Realisation	As at 23 Nov 2007 \$000's	Realisation 31 Jan 2008 \$000's	Revised \$000's
Cash at Bank	337	337	337
GST Refund	173	-	30
Accounts Receivable	1,997	-	-
Loans and Advances	182,597	43,662	24,028
Accrued Interest	1,364	-	-
Other Investments	4,996	-	-
Subsidiary	8,290	-	-
Taxation	(196)	-	30
Total Assets	199,558	43,999	24,425
Less Fortress	20,550	20,550	20,550
Available for Debenture Holders	179,008	23,449	3,875
Debentures	167,052	167,052	167,052
Surplus/(Shortfall) to Debenture Holders	11,956	(143,603)	(163,177)
Estimated Percentage Return to Debenture Holders prior to accrued interest and receivership costs.		14%	2%

Summary of Receivership Recoveries

From the Capital + Merchant Finance and CMI (Capital + Merchant) receiverships we have realised \$93.7 million to date from the companies' assets. Following this, we have paid prior chargeholders \$87 million, made up of:

	\$M
Fortress	61
Other prior Chargeholders	<u>26</u>
Total	<u>87</u>

If Fortress was included on the same priority ranking as the public debenture holders, the recoveries paid to investors in Capital + Merchant as a percentage of total debt is 25 cents in the dollar.

Effect of Insurance Policy or Legal Claims

In our estimates, we have not provided for any recovery from the insurance policy and legal claims against various parties as the recoveries, if any, cannot be reliably estimated.

Future Costs and Revenues

Interest continues to accrue on both loans and advances and amounts due to secured creditors. In addition, the estimated realisation figures are subject to costs.

Preferential Creditors

No amounts are owed to preferential creditors.

Unsecured Creditors

Based on the information we have, it appears that no funds will be available to meet the claims of unsecured creditors.

Receipts and Payments

The table opposite sets out the receipts and payments for the Company from 24 November 2008 to 23 May 2009.

We note the following in respect of the receipts and payments summarised in the table:

- From the 55 Loans, gross recoveries of approximately \$65.6 million had been realised as at 23 May 2009, with \$293k being realised in the last six months. Of this \$20.9 million has been repaid to Fortress; \$291k of this was paid in the last six months.
- Legal fees to date include general receivership advice, loan specific advice, property administration and transfer, and loan documentation.
- Insurance relates to the Lloyds policies and premiums paid in the period.
- Loan advances relate to ongoing costs incurred in order to complete recovery on the subsidiary company.
- Realisation costs include agent sales commissions, offshore legal fees, offshore government taxes, offshore council fees and settlement apportionments.

Capital + Merchant Finance Limited (In Receivership)	
Receivers' Receipts & Payments	
For the Period: 24-Nov-08 to 23-May-09	
	\$000's
Receipts	
Balance brought forward	50,392
Loan Settlements	293
Interest on DMT Notes	193
GST on Receipts	239
Income Tax Refund	30
Total Receipts	51,147
Payments	
Balance brought forward	50,416
GST Recoverable	12
GST Irrecoverable	4
Insurance	47
IT Related Costs	6
Legal Fees & Disbursements	20
Loan Advances	12
Realisation Costs	1
Receivers Fees & Disbursements	90
Secured Creditor Repayments - Fortress	291
Sundry Expenses	14
Valuation Fees	3
Total Payments	50,915
Net Funds on Hand	232

Investigations

As previously advised all records of the Company held at its premises were secured by us and a full back up of computer records was obtained immediately following our appointment.

There are a number of transactions, the appropriateness of which we are concerned about and we continue to investigate these along with agencies such as the Securities Commission, as referred to earlier in this report particularly in respect of “related party” transactions.

We are also aware of concerns raised by investors and other parties in respect of certain activities of the Company and certain parties, prior to the receivership.

As a result of the above investigations are taking place by various agencies in respect of the following:

- Specific transactions entered into by the Company prior to our appointment;
- The activities and conduct of the Company, the officers of the Company and third parties leading up to our appointment of Receivers;
- Any other matters that come to our attention, which we advised to other agencies.

Due to the legal consequences and the nature of these investigations, we are unable to provide details regarding these issues or our findings to date.

Appendix 1

Restrictions

All information contained in this report is provided in accordance with Sections 25 and 26 of the Receiverships Act 1993.

The statements and opinions expressed herein have been made in good faith, and on the basis that all information relied upon by us is true and accurate in all material respects, and not misleading by reason of omission or otherwise.

We have not independently verified the accuracy of the information provided to us, and have not conducted any form of audit in respect of the company. We express no opinion on the reliability, accuracy or completeness of the information provided to us and upon which we have relied. Whilst all care and attention has been taken in compiling this report, we do not accept any liability whatsoever arising from this report.

The statements and opinions expressed in this report are based on information available and assumptions made as at the date of this report. It is possible that actual outcomes may be significantly different from those disclosed in this report.

We reserve the right, but will be under no obligation, to review or amend our report, as additional information becomes available.

In addition the following should be noted:

- Certain values included in tables in this report have been rounded and therefore may not add exactly.
- All amounts are stated in New Zealand dollars.

Appendix 2

Directory

Capital + Merchant Finance	Capital + Merchant Finance Limited (In Receivership)
CMI:	Capital + Merchant Investments Limited (In Receivership)
DMT:	Diversified Mortgage Trust No 1 Limited
Fortress:	Fortress Credit Corporation (Australia) II Pty Limited, Level 43, 50 Bridge Street, Sydney, NSW 2000, Australia
Perpetual	Perpetual Trust Limited, Level 1 Pyne Gould Corporation Building, 233 Cambridge Terrace, Christchurch
Receivers:	Richard Simpson and Timothy Downes of Grant Thornton
Second Receivers:	Grant Graham and Brendan Gibson of Korda Mentha