IN THE COURT OF APPEAL OF NEW ZEALAND

CA832/2011
[2012] NZCA 155

BETWEEN	MARK STEPHEN HOTCHIN Appellant
AND	THE FINANCIAL MARKETS AUTHORITY Respondent

Hearing: 13 March 2012

Court: Randerson, Harrison and Wild JJ

Counsel: R B Stewart QC, N S Gedye and J A MacGillivray for Appellant
K P McDonald QC and G H Allan for Respondent

Judgment: 20 April 2012 at 10.30 am

JUDGMENT OF THE COURT

A The appeal is dismissed.

B The appellant is to pay the respondent costs for a standard appeal on a band A basis and the usual disbursements.

C Order under r 7(3) of the Court of Appeal (Access to Court Documents) Rules 2009 that the appeal file (except for the notice of appeal and any amended grounds of appeal) not be accessed without the leave of a Judge. No restriction on access to the formal Court record as defined by the Rules. There is no restriction on the publication of this judgment.

REASONS OF THE COURT

(Given by Wild J)

Introduction

[1] Mr Hotchin appeals against a judgment of Winkelmann J given in the Auckland High Court on 1 December 2011, following a hearing on 26 September.[1] The Judge declined Mr Hotchin's application to rescind interim asset preservation orders the Judge had made on 6 May 2011.[2] Those orders renewed, in amended terms, orders Winkelmann J had originally made in December 2010.[3]

[2] The original orders were made on the application of the Securities Commission (the Commission), the predecessor of the Financial Markets Authority (the FMA). Those orders had the purpose of ensuring that the rights of "aggrieved persons", as defined in s 60G(3) of the Securities Act 1978, were not frustrated by Mr Hotchin dissipating the assets, leaving them unavailable to meet claims against Mr Hotchin by the aggrieved persons.

[3] The nub of the appeal is that the Judge was wrong not to rescind the orders, and to accept undertakings from Mr Hotchin in their place.

Background

[4] The FMA has been investigating suspected breaches of the Securities Act by Mr Hotchin, in his capacity as a director of companies in the Hanover Finance Group (Hanover). Hanover failed in mid 2008 causing substantial losses to depositors.

[5] Following Hanover's collapse, the Commission began investigating potential breaches of the Securities Act by the directors of Hanover in respect of statements made in prospectuses Hanover had issued late in 2007 and in the early part of 2008. Approximately $32 million had been deposited with Hanover during this period.

[6] On 10 December 2010 Winkelmann J granted an ex parte application by the Commission for interim orders under s 60I of the Securities Act. The orders were against Mr Hotchin, two corporate trustees of trusts the Commission claimed held

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1 *Financial Markets Authority v Hotchin* HC Auckland CIV-2010-404-8082, 1 December 2011.
2 *Financial Markets Authority v Hotchin* [2011] 3 NZLR 469 (HC).
3 *Securities Commission v Hotchin* HC Auckland CIV-2010-404-8082, 21 December 2010.

assets in which Mr Hotchin had a beneficial interest, and also against Mr Thomas, the sole director and shareholder of those two corporate trustees. The trusts are KA No 4 Trustee Ltd (KA4) and KA No 3 Trustee Ltd (KA3).

[7] Winkelmann J amended the orders on 21 December 2010, following a hearing that day. The amended interim order against Mr Hotchin prohibited him from "transferring, charging, dealing or otherwise removing from New Zealand, money, securities and other property located in New Zealand that is held or controlled by him, whether legally or beneficially". There were exceptions, for example $1,000 per week for living expenses, and payment of reasonable legal and other expenses related to the proceeding.

[8] The amended interim orders against KA4 and KA3 and their director prohibited them, in similar terms, from dealing with assets held on behalf of Mr Hotchin.

[9] Also on 21 December 2010, Winkelmann J made orders under ss 65C or 65E of the Securities Act requiring Mr Hotchin to make an affidavit detailing his assets and liabilities. A related order was made against Mr Thomas.

[10] The interim preservation orders have been varied, and some of them rescinded, by Winkelmann J on successive occasions:

(a) 21 February 2011 — by consent, following a hearing on 14 and 15 February 2011;

(b) 6 May 2011 — in a lengthy judgment, also following the hearing on 14 and 15 February 2011;

(c) 2 November 2011 — following a hearing on 26 September and 2 November 2011; and

(d) 1 December 2011 — also following the hearing on 26 September and 2 November 2011.

[11] The general thrust of those variations was to facilitate payment of debts by Mr Hotchin, and to make the orders asset specific where possible. For example, in her 6 May 2011 judgment, Winkelmann J granted KA4's application for revocation of the existing orders, and substituted an order restricted to a property at 56 Paritai Drive in Auckland registered in KA4's name (Paritai Drive).

[12] In compliance with Winkelmann J's order, Mr Hotchin swore an affidavit on 28 January 2011 detailing his assets. At that point, he disclosed assets totalling approximately $4.4 million, but also listed liabilities of approximately $10.8 million.

[13] Mr Hotchin swore an affidavit on 25 January 2012 updating his asset position. Ms McDonald QC did not oppose our receiving this update, but she did object to the Court receiving another part of this affidavit. We deal with that in [38] below. In this latest affidavit Mr Hotchin discloses a negative asset position of approximately $8.3 million (assets worth $318,000; liabilities amounting to $8,620,000).

[14] The major liability Mr Hotchin deposed to was a debt of $8,490,214 to the KA No 2 Trust (KA2). Mr Hotchin stated that KA2 had made demand on him for payment. Subsequently, KA2 applied for summary judgment against Mr Hotchin in the High Court at Auckland. He filed an admission of the claim. On 29 February 2012 KA2 sealed judgment against Mr Hotchin in the sum of $8,490,214 together with interest and costs.

[15] We were informed by counsel that the FMA, having completed its investigation, had decided to file a civil proceeding against Mr Hotchin alleging breaches of the Securities Act. This proceeding was filed on 30 March.

The issues

[16] Although the parties framed them differently, they essentially agreed on four issues. Each is an aspect of the overriding issue: did Winkelmann J err in deciding that the preservation orders should remain, and in declining to replace them with

undertakings? It is convenient to deal with each of the four issues, before answering the overriding question posed by Mr Hotchin on this appeal.

Issue One. Assets: in light of Mr Hotchin's asset position, did the Judge err in holding that it was necessary to continue the preservation orders?

[17] Winkelmann J held:

> [15] Mr Hotchin says that since all assets, with the exception of any interest he has in the Paritai Drive property, have been or will be utilised in paying tax bills and other outgoings, there is little purpose to continuing the orders — they are a gross intrusion, while delivering little potential benefit for aggrieved persons. If it is true that the assets listed in his statement of assets and liability are now or shortly to be expended, the existence of the orders nevertheless continues to restrain dealings with the interest in the Paritai Drive property, and any also [sic] assets that come into Mr Hotchin's control in the future which are subject to the order, whether those derive from his own efforts, or from distributions from family controlled entities. Other than a reducing stock of assets there is nothing in the evidence to suggest that the assessment of potential for and risk of dissipation of assets set out in the earlier judgment has altered significantly.

[18] Mr Stewart QC accepted that the preservation orders were justified when made. That was because Mr Hotchin then had several million dollars of assets, which he might have sought to shift to Australia where he was living and working at the time. Mr Stewart did not challenge these findings by Winkelmann J:

(a) That there was no evidence of delay in the FMA's investigation.

(b) The existence of a prima facie substantive case which was serious, because of the number of potentially aggrieved persons and the amount they might become eligible to recover.

(c) The orders preserved, not only existing assets, but also assets acquired, and income earned, in the future.

(d) That there was an actual and on-going risk of dissipation of the existing assets, for the reasons given by the Judge.

[19] Pursuant to variation orders agreed to by the FMA, Mr Hotchin has applied most of the assets he held when the orders were made to pay his creditors. The largest of these was the Commissioner of Inland Revenue. Mr Hotchin has paid the Commissioner an agreed $3.13 million in three instalment payments, the last on 28 November 2011. Mr Stewart's submission was that the resulting gradual deterioration in Mr Hotchin's asset position to the point where he has only $300,000 in assets, and substantially greater liabilities, meant that the preservation orders no longer served any useful purpose. Indeed, Mr Stewart argued that they were counterproductive, in that they were preventing Mr Hotchin earning an income and restoring his asset position by employing his skills in property broking and dealing. We expand on this submission when dealing with issue three.

[20] On this appeal, for the first time, Mr Hotchin has offered to give expanded undertakings:

(a) In his January 2012 affidavit Mr Hotchin deposed:

> 38. If the Court is prepared to release the general preservation orders against me, I would be prepared to give undertakings that all existing specific assets as disclosed in my statement annexed hereto can be preserved for the FMA on the same terms as currently contained in the orders.

(b) As to future income/assets Mr Hotchin might acquire, Mr Stewart informed us from the bar that he was instructed to offer an additional undertaking, that Mr Hotchin will disclose to the FMA within a week any income/assets earned/acquired in excess of an agreed dollar limit.

(c) In respect of Paritai Drive, Mr Stewart further informed us that Mr Hotchin had instructed him to offer:

(i) To undertake not to deal with any interest he may have in the property without the prior written agreement of the FMA or order of the Court.

(ii) To assign his interest in the property (whatever it is) to the FMA by way of charge.

We revert to these newly offered undertakings in [22] and [27] below.

[21] We do not accept Mr Stewart's submission that the Judge erred in her assessment at [15] of her judgment. Our three reasons largely reflect Ms McDonald's submissions.

[22] First, the orders cover all assets, existing and future, and whether or not they have been disclosed by Mr Hotchin. The undertakings offered to the High Court do not. Nor, for that matter, do the undertakings detailed in [20] above.

[23] Secondly, given their nature, we accept Ms McDonald's submission that the liabilities deposed to by Mr Hotchin should not necessarily be deducted from his declared assets. We of course accept that the High Court has now entered judgment against Mr Hotchin in favour of KA2. But judgment was entered upon Mr Hotchin's admission of the claim. The provenance of this debt is not straightforward. In his 28 January 2011 affidavit, Mr Hotchin explained it thus:

> 5. In my first affidavit I explained that I owed a debt of approximately $6 million to [KA2]. In fact, after being briefed by my accountant, I can advise that the sum I owe is $7,588,397 as at the date of this affidavit. I borrowed this money personally from Hotchin Investments Limited, primarily to pay the construction costs at Paritai Drive.
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> 6. Hotchin Investments Limited assigned that debt to the Hotchin Trust, which in turn assigned it to [KA2] in reduction of a loan that the Hotchin Trust owed to [KA2]. That loan arose out of the restructuring of the various companies, which I describe in my affidavit in support of the application to rescind or vary the preservation orders. A copy of the deed of assignment of debt is [annexed].

The trust deed discloses that Mr Hotchin and his children are among the discretionary beneficiaries of KA2, which holds 50 per cent of the shares in Omara Properties Ltd. Mr Hotchin has deposed that he is the working director of this company. KA2 is not subject to the preservation orders, although Ms McDonald informed us that the FMA is considering this position.

[24] Thirdly, an interest in Paritai Drive appears, potentially, to be Mr Hotchin's major remaining asset. Ms McDonald advised us that the FMA will be claiming that

the full value of Paritai Drive — whatever it is — is an asset of Mr Hotchin, not just the $12.2 million approximately which Mr Hotchin deposed he paid toward the cost of building the Paritai Drive house.[4] The difference between the $12.2 million and the realisable value of Paritai Drive could be significant, because approximately $42 million will have been spent on the property by the time construction of the house is complete. We see no need in this judgment to delve further into the financial details of Paritai Drive, or into arrangements between Mr Hotchin and KA4 for a lease of it.

[25] Mr Stewart advised us that Mr Hotchin accepts that a separate proceeding will be necessary to determine the respective interests in Paritai Drive. We understand that KA4 intends to bring an appropriate proceeding. Further, on 18 October 2011, by consent, Venning J permitted KA4 to mortgage Paritai Drive to a sum not exceeding $4.5 million, in order to raise the monies necessary to complete building the house. The aim of that is to realise the value of Paritai Drive to best advantage.

[26] In the light of all this, Winkelmann J was certainly not in error in considering that an order preserving Paritai Drive was still necessary.

[27] The undertakings we have set out in [20] above, offered by Mr Hotchin in this Court for the first time, may or may not at some future point be adequate substitutes for the interim orders. For the reasons we elaborate on in [45], we consider any decision on that is appropriately and best made by Winkelmann J. For the present, we agree with the Judge that the current orders continue to be required. The date for completion of the construction of Paritai Drive is unknown, although it is likely to be some time away. As well, the nature of any interest Mr Hotchin may have in Paritai Drive and K4 remains unclear.

[28] Before leaving Paritai Drive, we record our concern that the preservation order as it applies to Paritai Drive should be expanded so as explicitly to prevent KA4 releasing any debt it owes Mr Hotchin in respect of Paritai Drive, or otherwise

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[4] At [4.3] of the affidavit he swore on 28 January 2011.

entering into any arrangement with Mr Hotchin in respect of his interest in Paritai Drive.

Issue Two. Undertakings: did the Judge err in holding they would not provide satisfactory protection?

[29] Winkelmann J held:

> [16] Mr Hotchin asks that the orders be discharged because the existence of the orders is damaging his ability to earn a living, and in that sense is counter-productive. It is difficult to see how the situation he describes will be improved by the substitution of undertakings in terms identical to the existing orders. Undertakings will also provide a less satisfactory protection for aggrieved persons. If an undertaking is breached, the FMA would have to seek an order compelling compliance. If it were too late for that, proceedings for contempt of court would likely be the best remedy. In contrast, there is very real sanction for breach of orders made under the Securities Act 1978. A person who breaches an order made under s 60H or s 60I commits an offence under s 60K of the Act and is liable on conviction on indictment to imprisonment for a term not exceeding 3 years or to a fine not exceeding $100,000, or both.

[30] Mr Stewart's criticisms of this part of the judgment were two-fold. First, he submitted that the Judge gave inadequate consideration to the difficulties the preservation orders posed for Mr Hotchin, in terms of his ability to earn a living. That is issue three, and we deal with it there.

[31] Secondly, Mr Stewart submitted that Winklemann J had not considered comparable Australian authority, in terms of the adequacy of undertakings. He referred us to two Australian cases. The first is the judgment of French J in the Federal Court in *Australian Securities and Investments Commission v Carey (No 21).*[5] French J was dealing with the extension of protective orders comparable to those in issue here. He reiterated the purpose of the orders (20 previous judgments had been given in the proceeding), and recorded that the Australian Securities and Investments Commission (ASIC) had originally applied for a two and a quarter year extension of the orders. He then recorded that it was now accepted that the orders should continue to apply for just over three months, to the end of June

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5 *Australian Securities and Investments Commission v Carey (No. 21)* [2008] FCA 381.

2008, by which date the ASIC anticipated completing its investigation. He then said this:

> [7] The extension of the orders being justified to 30 June, it is within my power to accept undertakings offered in lieu of the orders which would otherwise be made. An undertaking accepted by the Court has the force of an injunction as against the party making the undertaking. The Court will not accept an undertaking unless it is satisfied that it would have the power to make an order in those terms and that such an order would be, in a broad sense, appropriate. I am satisfied that the undertakings which are offered, which have been the subject of significant negotiation between ASIC and various parties affected, are within power and are appropriate. Copies of the undertakings are annexed to these reasons.

[32] The other case is the judgment of Santow J in the Supreme Court of New South Wales in *Australian Securities and Investments Commission v Adler*.[6] The judgment is a short one in which Santow J gave brief reasons for earlier declining to make the orders sought on an ex parte basis, and for now accepting the undertakings proffered. The judgment concludes:

> [9] In all the circumstances, the proffering of undertakings without admission which have satisfied ASIC is to be welcomed. For the future, and recognising that circumstances may change, I have given leave to all parties to approach the court at short notice.

[33] As Ms McDonald pointed out, these two decisions, certainly *Adler*, instance the Court accepting undertakings with the agreement of the ASIC. Such agreement is not forthcoming from the FMA in this case. The bare fact that the ASIC agreed to the Court accepting undertakings in *Carey (No 21)* and in *Adler* provides scant, if any, support for Mr Stewart's submission that the FMA should agree to accept undertakings in this case.

[34] It is significant that Mr Stewart did not contend that Winkelmann J erred in enunciating the principles relating to asset preservation orders. Indeed, he expressly took no issue with the Judge's summary of those principles in her 6 May 2011 judgment.[7] In the course of that summary, Winkelmann J referred to a number of the Australian cases, including *Adler*.[8] Particularly relevant to Mr Stewart's challenge to

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6 *Australian Securities and Investments Commission v Adler* [2001] NSWSC 451, (2001) 38 ACSR 266.

7 At [47]–[60].

8 At [55] and [57].

Winkelmann J's judgment of 1 December last, are these principles mentioned by the Judge in her 6 May 2011 judgment:

(a) Even if made on an interim basis, preservation orders are a significant interference with property rights, and the Court should exercise care before making any orders.[9]

(b) The FMA applies for preservation orders on behalf of aggrieved persons. This public interest role may warrant an order in circumstances where it might be denied to a private litigant. However care must be taken not to attach too much weight to this factor, as to do so risks effectively substituting the FMA's assessment of what is necessary or desirable for that of the Judge.[10]

(c) The jurisdiction is not to be exercised for a disciplinary purpose. Any orders must be made for the purpose of preserving assets that could be available to meet any judgment ultimately entered against the liable person. For this reason, if orders are made, the Court must ensure that the orders are no more intrusive than required to preserve the assets.[11]

[35] In [16] of the judgment under appeal, Winkelmann J observed that undertakings would provide a less satisfactory protection for aggrieved persons than do orders in terms of sanctions. The Judge pointed out that a person who breaches a preservation order is liable upon conviction on indictment to both imprisonment for up to three years and a fine not exceeding $100,000. By contrast, the sanction for breach of an undertaking to the High Court is committal for contempt, and the Court can impose a sentence of imprisonment for contempt of no more than three months and/or a fine: *Siemer v Solicitor-General*.[12]

[36] We agree with the Judge that the sanctions under the Securities Act provide a considerably more powerful sanction for non-compliance with the orders than would

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9 At [50].
10 At [57].
11 At [60].
12 *Siemer v Solicitor-General* [2010] NZSC 54, [2010] 3 NZLR 767 at [67].

be available in the event of a breach of a personal undertaking. Another advantage of preservation orders is that they enable more effective supervision by the Court than would be the case if undertakings were given. A proceeding under the Securities Act is brought in the public interest and Court oversight of the proceeding is vital in ensuring that the public interest is protected, while at the same time proper weight is given to the interests of those facing the proceeding.

Issue Three. Mr Hotchin's ability to earn a living: did the Judge err in her assessment of the effect of the orders on this?

[37] The Judge deals with this in the first two sentences of [16] of her judgment, set out in [29] above. Earlier, Winkelmann J had recorded:

> [5] Mr Hotchin has filed affidavits in which he has described the effect of the existing orders on him and his family. The family remains subject to the stresses that are also described in earlier affidavits and which are outlined in my May judgment. Mr Hotchin says that the orders have prevented him from earning income as no one wishes to deal with him whilst he remains subject to them. Because of this, the family's financial resources have been exhausted, with almost nothing remaining of an Australian bank account which is outside the scope of the orders, and which the family have been using for their expenses. Mr Hotchin has been forced to rely upon family for financial support. The existing orders allow him living expenses of $1,000 per week. Earlier when he made an application for an increase in the amount allowed for living expenses, private details in relation to his family's living expenses detailed in his affidavit were reported by the media. Therefore, although he knows that he can apply to increase the amount of the allowance, he has not done so.

[38] Mr Hotchin's January 2012 affidavit contains a section headed "Effect of preservation orders on my ability to earn a living". The FMA objected to this part of the affidavit, on the ground that it failed to meet the well established principles for admission of further evidence in support of an appeal.[13] Viewing the impugned part of Mr Hotchin's affidavit as favourably as we can from his viewpoint, we do not think it is fresh evidence and decline to admit it. Although some of the dates he gives are vague,[14] we view the evidence as an amplification of what was, or should have been, before Winkelmann J at the hearing on 26 September 2011.

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13 These are summarised in *McGechan on Procedure* (looseleaf ed, Brookers) at [CR45.01–02].

14 For example, "later in 2011", at [25].

[39] We also see force in the FMA's submission that we should be particularly cautious about receiving further evidence in support of this appeal, because the High Court is anything but functus officio. Under s 65E(2) of the Securities Act, the High Court is empowered to "revoke, vary, or suspend" preservation orders, and Winkelmann J has exercised that power several times. So fresh evidence can and should be directed to the High Court and not to this Court in support of an appeal. Even if we were to receive the impugned fresh evidence, there is substance in the FMA's objection that the hearsay nature of much of that evidence detracts from its force.

[40] The end result of all this is that we cannot fault Winkelmann J's assessment that it is difficult to see how the substitution of undertakings in terms identical to the existing orders will improve Mr Hotchin's situation. Indeed, in the challenged part of his affidavit, Mr Hotchin does not actually say that undertakings will overcome his difficulties. He merely deposes to difficulties resulting from the preservation orders remaining in place.

[41] We accept Ms McDonald's submission that any stigma arising from the preservation orders will anyway arise by reason of the substantive proceeding the FMA is to bring against Mr Hotchin.

Issue Four. Future assets or income: did the Judge err in finding that the possibility of these justified continuation of the orders?

[42] In [15] of her judgment, set out in [17] above, Winkelmann J noted that the orders catch any assets that come into Mr Hotchin's control in the future, whether they derive from his own efforts or from distributions from family controlled entities. In the preceding paragraph in her judgment, Winkelmann J said this:

> [14] Mr Hotchin has argued that the existing orders do not extend to future assets in the sense of future income. However the orders are clearly enough expressed to extend to income and other assets of Mr Hotchin which are situated in New Zealand, whether acquired before or after the making of the orders. This is of course consistent with the intention to preserve assets to meet any judgment against Mr Hotchin, should proceedings be issued against him. For this reason, I also decline to amend the orders to expressly exclude future acquired property, as Mr Hotchin had invited me to if I came

> to the view that in their present form the existing orders caught such property.

[43] Mr Stewart submitted that there was no evidence before the High Court of any specific future assets or income which Mr Hotchin expected or was entitled to receive or acquire. Mr Hotchin accepted that some control was required over future assets or income, but submitted that the undertaking we have summarised in [20](b) above adequately preserved any future assets or income. This is essentially the point we have dealt with under issue two over again. We need not answer it a second time.

[44] Mr Stewart accepted that, if Mr Hotchin had a specific proposal to put forward in relation to future assets and income, he was able to apply to the High Court to vary its orders.

Generally

[45] A point rightly emphasised by the FMA is the importance of the High Court's supervisory jurisdiction of the orders, under s 65E(2) of the Securities Act. Winkelmann J has exercised that supervision since she made the orders, ex parte, on 9 December 2010. If the Australian jurisprudence demonstrates one thing, it is the advantage of one Judge supervising orders such as those in issue here. That gives the supervising Judge a depth, breadth and constancy of overview that an appellate Court cannot emulate. We accept — as did Mr Stewart — that Winkelmann J was correct, in her 6 May 2011 judgment, in describing the s 60I jurisdiction in these terms:[15]

> [53] In determining whether it is necessary or desirable to make the orders sought, the court must undertake an evaluative exercise. It is left to the court to determine what matters to take into account but it is clear that there is an element of risk management or risk assessment involved in determining whether it is necessary or desirable that orders be made.

[46] We have already held against Mr Hotchin on each of the four issues put to us. Taking an overall view, we are not persuaded that Winkelmann J erred in her evaluation that the orders were still necessary and appropriate, and that the undertakings proffered to her by Mr Hotchin were not a satisfactory substitute.

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[15] Footnotes omitted.

[47] In [28] we have suggested a clarification of the order relating to Paritai Drive. We also commend consideration of a variation that would enable the orders to be altered in a manner agreed to by the FMA, without the need for Mr Hotchin to apply to the High Court. There is force in Mr Stewart's complaint that application is an unnecessary cost if the variation sought is by consent. Obviously, a minuting to the Court of the agreed variation would be required, so that Winkelmann J was informed of the position.

Result

[48] The appeal is dismissed.

[49] The appellant is to pay the respondent costs for a standard appeal on a band A basis and the usual disbursements.

[50] The High Court made an order restricting access to the Court file. Without opposition by the FMA, we make an order under r 7(3) of the Court of Appeal (Access to Court Documents) Rules 2009 that the appeal file not be accessed without the leave of a Judge. There is no restriction on access to the formal Court record as defined by the Rules, but we also exclude from the order the notice of appeal and any amended grounds of appeal. There is no restriction on the publication of this judgment.

Solicitors:
Tompkins Wake, Hamilton for Appellant
Crown Law Office, Wellington for Respondent