

# Settlement Agreement

Financial Markets Authority

Prince & Partners Trustee Company Limited

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## Parties

Financial Markets Authority (FMA)

Prince & Partners Trustee Company Limited (Prince)

## Introduction

### Background

- A Prince was a professional corporate trustee, appointed as a trustee in respect of debt securities issued by the finance company Priority Finance Limited (**Priority**), later renamed Viaduct Capital Limited (**Viaduct**), under a Debt Security Trust Deed dated 6 October 2006 (**Trust Deed**). Priority's primary activity was to lend money secured by residential and commercial property. It raised funds by offering debt securities to the public.
- B Under the Trust Deed, Prince agreed to act as trustee for the benefit of and to protect the interests of holders of those debt securities (**investors**).
- C Priority entered into a Crown Deed of Guarantee with the Crown (**Crown Guarantee**) on 13 November 2008.
- D Prince owed investors a duty to carry out its functions as a trustee with the skill, care and diligence to be expected of a reasonably competent and prudent professional trustee.
- E Prince had a duty to exercise reasonable diligence to ascertain whether or not:
  - a. Viaduct had committed any breach of the provisions of the Trust Deed or terms of offer of the debt securities; and
  - b. the assets of Viaduct were sufficient or likely to be sufficient to discharge the amounts of the debt securities as they became due.
- F In February 2009, Prince approved a transaction in which Priority was sold to new owners and management.
- G In April 2009, following two investigation reports from PwC into the affairs of Viaduct, Treasury withdrew Viaduct's Crown Guarantee.
- H By statement of claim dated 13 August 2014, the FMA commenced proceedings under s 34 of the Financial Markets Authority Act 2011 (**FMA Act**) against Prince in the High Court of New Zealand, Auckland Registry (CIV-2014-404-2026) (**Proceeding**).
- I FMA claims that Prince failed to fulfil its obligations to investors in respect of the Acquisition Transaction and the withdrawal of the Crown Guarantee as detailed further in paragraphs J, K and L below (**Claims**).
- J FMA claims that Prince caused loss to investors by approving the Acquisition Transaction that was not in the best interests of the investors.

- K In relation to the withdrawal of the Crown Guarantee, FMA claims that Prince caused loss to investors by failing to exercise its powers of enforcement when put on notice of an event of default under the Trust Deed.
- L The FMA claims that reasonable diligence by Prince in fulfilling its obligations required:
- a. more than passive acceptance of information provided by the directors of Viaduct or third parties;
  - b. consideration of that information together with independent enquiries and a degree of professional scepticism; and
  - c. intervention using the powers granted to the trustee, under the Trust Deed and at law, to prevent, or mitigate the risk of, prejudice to investors.
- M The FMA and Prince have agreed to settle the Claims and the Proceeding and matters arising from them on the terms set out in this Agreement (**Agreement**).

## 1 Admissions

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- 1.1 Prince makes the admissions set out in **Schedule One** to this Agreement. In summary, Prince has admitted:

### *Acquisition Transaction*

- (a) Prince did not:
- (i) make adequate inquiries or seek independent legal and accounting advice or take steps to ensure that the Acquisition Transaction and the nature of the relationship between Hunter Capital Group Limited and Viaduct was disclosed to investors;
  - (ii) exercise the level of professional scepticism required in the circumstances and should have required further information or undertaken further enquiries before it consented to the Acquisition Transaction.
- (b) The Acquisition Transaction was not in the best interests of investors, and adversely affected their interests and increased the risk that the assets of Viaduct would not be sufficient to discharge Viaduct's debt securities as they became due.

### *Withdrawal of Crown Guarantee*

- (c) Prince did not:
- (i) make further inquiries to ascertain whether there were any breaches of the Trust Deed or the terms of the offer of Viaduct's debt securities;
  - (ii) exercise the level of professional scepticism required in the circumstances;
  - (iii) make further inquiries to ascertain whether the assets of Viaduct would be sufficient or likely to be sufficient to discharge the amounts of the debt securities as they became due; and

- (iv) consider the merits of allowing Viaduct to continue trading and soliciting funds from the public.
- (d) If, following receipt of the PwC Reports and notice of the withdrawal of the Crown Guarantee, Prince had taken steps to investigate the possible breaches of the Trust Deed and to independently monitor the financial position of Viaduct, this may have resulted in it exercising its rights under the Trust Deed earlier, which would have better protected the interests of investors.

## **2 Terms of Settlement**

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- 2.1 This Agreement is conditional upon the High Court's approval of the Agreement as required under s 41 of the FMA Act (**Court's Approval**).

### *Settlement sum*

- 2.2 Prince will pay the FMA a total sum of NZD \$4.5 million (GST inclusive if any) (**Settlement Sum**) no later than five (5) working days after the date of the Court's Approval.
- 2.3 The Settlement Sum shall be paid without set-off or deduction by depositing cleared funds into a bank account to be nominated by the FMA. Payment will be effective upon confirmation by the receiving bank of the deposit of cleared funds into the relevant account.

### *Undertaking not to act as supervisor of regulated offer of debt securities*

- 2.4 Prince agrees not to act as supervisor of any regulated offer of debt securities for a period of five years from the date of this Agreement.

### *General*

- 2.5 In consideration of payment of the Settlement Sum all and any claims by the FMA against Prince and/or the directors/shareholders of Prince for any losses, damages, costs or liabilities suffered or incurred in relation to the Claims and/or the Proceeding are fully settled.
- 2.6 The FMA will file a notice of discontinuance of the Proceeding after confirmation of the receipt of the Settlement Sum in accordance with clause 2.3.
- 2.7 The parties agree that costs in the Proceeding and in relation to this Agreement are to lie where they fall.
- 2.8 The parties will generally co-operate and do all things reasonably necessary to give effect to the terms of this Agreement including preparing, signing and filing an executed notice of discontinuance and provide such assistance as is reasonably required in relation to obtaining the Court's Approval.

### **3 Default**

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- 3.1 In the event that Prince fails to pay the Settlement Sum within the time required under clause 2.2, the FMA may at its absolute discretion:
- (a) enforce this Agreement and pursue recovery of the Settlement Sum plus interest (at 5 per cent per annum) and legal costs on a solicitor-client basis; or
  - (b) give notice of intention to cancel the Agreement under clause 3.2.
- 3.2 In the event of default under clause 3.1 and if it elects to cancel the Agreement under clause 3.1(b), the FMA shall give notice of its intention to cancel the Agreement and pursue the Claims if Prince's default is not remedied within a period of not less than two (2) working days.
- 3.3 Following the expiry of a notice of intention to cancel this Agreement under clause 3.2, if Prince has not paid the Settlement Sum together with accrued interest in full, the FMA at its absolute discretion may cancel this Agreement and pursue the Claims and Proceeding against Prince as if this Agreement had not been entered into.

### **4 Confidentiality**

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- 4.1 The fact and terms of this Agreement, including the admissions, are not confidential and may be disclosed by the parties.
- 4.2 The parties agree that following the Court's Approval the FMA may make a public announcement that the settlement has been reached and may post a copy of this Agreement on its website.
- 4.3 Subject to the terms of this Agreement, all materials exchanged between the parties during all without prejudice negotiations, shall retain their privileged and confidential character.
- 4.4 All materials produced and obtained by the FMA and any of its advisors, during the investigation of Prince as well as during the Proceeding, shall retain any confidential or privileged character that they may have.

### **5 Entire agreement**

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- 5.1 This Agreement constitutes the entire agreement between the parties with respect to the subject matter of the Proceeding and the Claims, and replaces all earlier negotiations, representations, warranties, understandings and agreements, whether oral or written, between the parties with respect to the matters that are the subject of this Agreement.
- 5.2 The parties acknowledge that neither party has been induced to enter into this Agreement by any representation, express or implied, made by the other party. Neither party may cancel this Agreement or be entitled to damages on account of any misrepresentation alleged to arise from or in connection with any such representation.
- 5.3 The provisions of this Agreement shall bind the parties in all respects and each party hereto accepts the risk of mistake in respect of all matters relevant to this settlement

and hereby is obliged to assume such risks for the purposes of section 6(1)(c) of the Contractual Mistakes Act 1977.


## **6 General**

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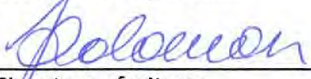
- 6.1 **Counterparts:** This Agreement may be executed in any number of counterparts (including facsimile and/or pdf copies) and provided that every party has executed a counterpart, the counterparts together shall constitute a binding and enforceable agreement between the parties.
- 6.2 **Further assurance:** Each party shall make all applications, execute all documents, and do all acts and things necessary to implement and to carry out its obligations under this Agreement.
- 6.3 **Modification:** No amendment or modification of any provision of this Agreement shall be valid unless it is in writing and signed by the parties.
- 6.4 **Authorities:** Each person executing this Agreement warrants that he or she has full authority to enter into the Agreement and/or notice of discontinuance and bind the parties on behalf of whom he or she purports to execute this Agreement and/or the notice of discontinuance.
- 6.5 **Time of the essence:** Time shall be of the essence for any times or dates contained in this Agreement.
- 6.6 **Severance:** The illegality, invalidity or unenforceability of any provision of this Agreement shall not affect the legality, validity or enforceability of any other provision.
- 6.7 **Governing law:** This Agreement shall be governed by and construed in accordance with the laws of New Zealand.
- 6.8 **Jurisdiction:** The parties irrevocably submit to the exclusive jurisdiction of the courts of New Zealand with respect to any dispute, legal action, suit or proceeding or any other matter directly indirectly arising out of or in connection with this Agreement.

**Execution**

Signed by and on behalf of **Financial Markets Authority** by its Chief Executive Officer **Rob Everett** in the presence of:

  
\_\_\_\_\_  
Rob Everett

Witness to signature:

  
\_\_\_\_\_  
Signature of witness

  
\_\_\_\_\_  
Name of witness

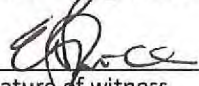
  
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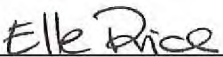
  
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City/town of residence

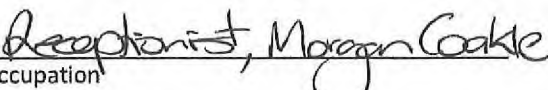
Signed by and on behalf of **Prince & Partners Trustee Company Limited** by **Colin Wilson** in the presence of:

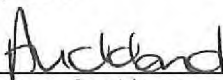
  
\_\_\_\_\_  
Colin Wilson

Witness to signature:

  
\_\_\_\_\_  
Signature of witness

  
\_\_\_\_\_  
Name of witness

  
\_\_\_\_\_  
Occupation

  
\_\_\_\_\_  
City/town of residence



## Schedule One: Admissions

In relation to FMA's claim in proceeding CIV 2014 – 404 - 2026 Prince & Partners Trustee Company Limited (Prince) admits as follows:

### 1 Background

- 1.1 Prince was a professional corporate trustee, appointed as a trustee in respect of debt securities issued by the finance company Priority Finance Limited (**Priority**), later renamed Viaduct Capital Limited (**Viaduct**), under a Debt Security Trust Deed dated 6 October 2006 (**Trust Deed**). Priority's primary activity was to lend money secured by residential and commercial property. It raised funds by offering debt securities to the public.
- 1.2 Under the Trust Deed, Prince agreed to act as trustee for the benefit of and to protect the interests of holders of those debt securities (**investors**).
- 1.3 Priority entered into a Crown Deed of Guarantee with the Crown (**Crown Guarantee**) on 13 November 2008.
- 1.4 Prince admits that it owed investors a duty to carry out its functions as a trustee with the skill, care and diligence to be expected of a reasonably competent and prudent professional trustee.
- 1.5 Prince admits that it had a duty to exercise reasonable diligence to ascertain whether or not:
  - (a) Viaduct had committed any breach of the provisions of the Trust Deed or terms of offer of the debt securities; and
  - (b) the assets of Viaduct were sufficient or likely to be sufficient to discharge the amounts of the debt securities as they became due.

### 2 Acquisition transaction

- 2.1 On 13 February 2009, Priority was acquired by a newly formed company called Phoenix Finance Holdings Limited (**Phoenix**). The director and ultimate shareholder of Phoenix was Nick Wevers, who was also the Chief Executive of Hunter Capital Group Limited (**Hunter Capital**), which was owned and controlled by Paul Bublitz. The overall structure of the transaction was that:
  - (a) Hunter Capital would sell four assets to Priority in return for cash and capital notes issued by Priority; and
  - (b) Hunter Capital would then provide a loan to Phoenix to enable it to settle the purchase with the shareholders of Priority (**Acquisition Transaction**).
- 2.2 On 9 February 2009, Prince received information relating to the Acquisition Transaction, including:
  - (a) A memorandum that summarised the Acquisition Transaction.
  - (b) A draft sale and purchase agreement, which provided that the Acquisition Transaction was conditional on Prince approving it.

- (c) A legal opinion from DLA Phillips Fox, which was addressed to Prince, as well as to the directors of Priority and its auditors, BDO, which advised that, based on certain assumptions provided by Hunter Capital, the proposed transaction was not technically a related party transaction.
  - (d) Briefing papers on the four assets owned by Hunter Capital to be sold to Priority as part of the Acquisition Transaction, which included independent valuation figures for each of the assets by, variously, Jones Lang La Salle, DTZ, and Seagar and Partners, supporting the purchase price of the assets.
- 2.3 On 10 February 2009, Nick Wevers, on behalf of Hunter Capital, sent to Prince an email attaching a draft approval letter for Prince to sign. Two days later, on 12 February 2009, Prince signed that it approved the Acquisition Transaction.
- 2.4 In approving the Acquisition Transaction, Prince relied on information provided to it by Priority and Hunter Capital and the DLA Phillips Fox opinion and did not undertake separate inquiries or due diligence into whether the transaction complied with the Trust Deed or was otherwise in the interests of investors. In particular, Prince did not:
- (a) make adequate inquiries into the relationship between Nick Wevers, Paul Bublitz and Hunter Capital;
  - (b) seek independent legal and accounting advice on any possible breaches of the Trust Deed or the Crown Guarantee given that no independent party examined the Acquisition Transaction (and the opinions by DLA Phillips Fox prior to the Acquisition Transaction were prepared on Hunter Capital's instructions, and relied on documents provided by Hunter Capital);
  - (c) make adequate inquiries into the assumptions relied upon by DLA Phillips Fox, particularly that the parties were not related and that the purchase price had been determined on an arms length commercial basis;
  - (d) after the Acquisition Transaction, take steps to ensure that the Acquisition Transaction and the nature of the relationship between Hunter Capital Group Limited and Viaduct was disclosed to investors in Viaduct's prospectus dated 3 March 2009, as recommended by DLA Phillips Fox;
  - (e) consider adequately what effect Viaduct's issue of capital notes to Hunter Capital would have on:
    - (i) Viaduct's compliance with its financial covenants under the Trust Deed; and
    - (ii) whether the assets of Viaduct would be sufficient or likely to be sufficient to discharge the amounts of Viaduct's debt securities as they became due;
  - (f) carry out adequate due diligence on Hunter Capital's financial position in order to assess its ability to meet the put options and indemnities provided as part of the Acquisition Transaction;
  - (g) make adequate inquiries into Priority's purchase of shares as part of the Acquisition Transaction, particularly where such share purchase:
    - (i) was not in the ordinary course of business of Viaduct as set out in its most recent prospectus at the time;

- (ii) was contrary to the statements in that prospectus as to what investor funds would be used for; and
- (iii) concerned the purchase of an illiquid asset of uncertain value.

2.5 While it considered the Acquisition Transaction to be satisfactory at the time, Prince admits that the Acquisition Transaction was not in the best interests of investors, and adversely affected their interests. In particular, it led to the withdrawal of the Crown Guarantee and increased the risk that the assets of Viaduct would not be sufficient to discharge Viaduct's debt securities as they became due.

2.6 Overall, Prince did not exercise the level of professional scepticism required in the circumstances and should have required further information or undertaken further enquiries before it consented to the Acquisition Transaction.

### 3 Withdrawal of Crown Guarantee

3.1 On 16 February 2009, Priority was renamed Viaduct and it purchased four further assets from Hunter Capital in exchange for \$1.5 million in capital notes (**16 February transaction**).

3.2 On 16 March 2009, Prince received a copy of Treasury's letter to Viaduct's directors raising significant concerns about the Acquisition Transaction and transactions that were or could become related party transactions.

3.3 Around 18 March 2009, Treasury appointed PwC to investigate the Acquisition Transaction and the 16 February transaction.

3.4 PwC issued reports (20 March 2009 interim report and 15 April 2009 final report), which were provided to Prince, detailing its investigation (**PwC Reports**) and which referred to concerns about:

- (a) the source of funding for the Acquisition Transaction;
- (b) the 16 February transaction;
- (c) the lack of due diligence undertaken by Viaduct and its directors in respect of the assets purchased by Priority from Hunter Capital and whether this was consistent with statements in Viaduct's most recent prospectus about its credit approval and loan management process;
- (d) a management agreement entered into by Viaduct with Paul Bublitz of Hunter Capital;
- (e) the capital notes issued to Hunter Capital (if all were converted to equity when they fell due in February 2010 Hunter Capital would have an approximately 70 per cent shareholding in Viaduct);
- (f) the shares in Priority being sold to Phoenix at a premium;
- (g) the value of one of the assets acquired in the Acquisition Transaction potentially having declined since the date of the valuation relied on;
- (h) some of the loans forming part of the Acquisition Transaction being structured as distinct loans, but being identical in all other material respects. If these

were in fact one loan, it would exceed the exposure limit restrictions of the Trust Deed;

- (i) the Acquisition Transaction and the 16 February 2009 transaction representing a significant departure from Viaduct's previous manner of business and from how its business was described in its prospectus;
- (j) recovery of one of the loans subject of the Acquisition Transaction being questionable;
- (k) the asset purchases by Viaduct appearing to have coincided with a desire by Hunter Capital to exit a number of its investments; and
- (l) as a consequence of the Acquisition Transaction, cash in Viaduct being used to purchase assets with limited liquidity, resulting in a decrease in cash from around \$2.8 million to \$231,000.

3.5 As a result of the PwC Reports, Treasury withdrew the Crown Guarantee from Viaduct on 20 April 2009. In doing so, Treasury advised Viaduct that it considered that the benefit of the Crown Guarantee was being extended to persons not intended to receive that benefit, namely Mr Bublitz and Hunter Capital, and was otherwise inconsistent with the intentions of the Crown in entering into the Crown Guarantee.

3.6 Prince received copies of the PwC Reports, and notice of the withdrawal of the Crown Guarantee and the reasons for it. Prince also received and relied on a copy of the responses by the directors of Viaduct to the PwC Reports and was advised by the directors of Viaduct that they considered the withdrawal of the Crown Guarantee was not justified.

3.7 As at 20 April 2009, Viaduct had over \$6 million cash reserves, and the total value of cash reserves, finance receivables and shares exceeded the amounts then outstanding to investors.

3.8 On 24 April 2009 and 8 June 2009, Viaduct made amendments to its registered prospectus disclosing the withdrawal of the Crown Guarantee and providing details of the reasons for it, including the concerns raised in the PwC Reports.

3.9 On 31 August 2009, Viaduct filed its financial statements for the year ended 31 March 2009. These included an unqualified audit opinion from Viaduct's auditors, BDO, as at 31 August 2009. BDO provided a further unqualified audit opinion on 9 October 2009 which was included in the Viaduct registered prospectus of that date.

3.10 Throughout the period from 28 February 2009 to 31 March 2010 the directors of Viaduct issued monthly and quarterly reports to Prince confirming that there had not been any event materially affecting the ongoing operation of Viaduct.

3.11 On or about 13 May 2010, on being advised that Viaduct was insolvent, Prince appointed McDonald Vague as receivers of Viaduct.

3.12 The FMA considers, and Prince admits, that the PwC Reports and the subsequent withdrawal of the Crown Guarantee indicated possible breaches of the Trust Deed and potential liquidity issues that threatened Viaduct's future ability to discharge the amounts of the debt securities as they became due.

3.13 Prince admits that if, following receipt of the PwC Reports and notice of the withdrawal of the Crown Guarantee, it had taken steps to investigate the possible

breaches of the Trust Deed and to independently monitor the financial position of Viaduct, rather than relying on the monthly and quarterly reports provided to it by the directors of Viaduct and on the unqualified audit reports by BDO dated 31 August 2009 and 9 October, then this may have resulted in it exercising its rights under the Trust Deed earlier, which would have better protected the interests of investors. In particular, Prince did not:

- (a) make further inquiries to ascertain whether there were any breaches of the Trust Deed or the terms of the offer of Viaduct's debt securities;
- (b) assess independently and objectively Viaduct's grounds in support of their intention to challenge the Crown's decision to withdraw the Crown Guarantee and exercise the level of professional scepticism required in the circumstances;
- (c) make further inquiries to ascertain whether the assets of Viaduct would be sufficient or likely to be sufficient to discharge the amounts of the debt securities as they became due; and
- (d) consider the merits of allowing Viaduct to continue trading and soliciting funds from the public.

#### **4 Receivership**

4.1 As at receivership, the total amount outstanding to investors was:

- (a) around \$7.3 million (including interest accrued) of investments made prior to the withdrawal of the Crown Guarantee;
- (b) around \$515,000 (including interest accrued) of investments made after the withdrawal of the Crown Guarantee.