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Court clarifies powers to freeze assets in high profile case

The interim freezing orders made against Mark Hotchin's New Zealand assets in December and the subsequent application by Mr Hotchin and two family trusts associated with him to have those orders overturned have drawn the courts into new territory.

Such orders are rare and were described by Winkelmann J, the presiding Judge in the proceedings, as "drastic". Yet there is the potential that they will be sought more often in the future because they can now be made across a wider catchment.

The purpose of the orders is to protect the rights of aggrieved investors to damages, compensation or restitution by preventing a potentially liable person from organising their assets to remove them from the reach of the regulator and from any other claim.

Previously orders could be made only in relation to breaches under the Securities Act and the Securities Markets Act and for non-compliance with the Takeovers Act or Code.

However they now apply to any of the financial markets legislation under the oversight of the Financial Markets Authority *(FMA)*. This includes the Companies Act and Financial Reporting Act and a broad range of potential proceedings, including where the FMA might elect to exercise a person's right of action such as a company's claim for breach of directors' duties.

Given this extension of jurisdiction, it is useful that the Court has now turned its mind to how the power should be applied. Although the provisions have been on the statute books in New Zealand since 2006, the Hotchin litigation was the first time that the Courts had been invited to rule on them. The Judge drew heavily on Australian precedent in distilling the following "principles":

- Orders can be granted in investigations where breaches have not yet been established "and even where no decision has been taken to bring proceedings".
- Even if made on an interim basis, the orders represent a significant interference with property rights so the Court should exercise care in their use, while also being mindful that Parliament clearly intended that "drastic remedies should be available".

- The Court has to be satisfied only that the intervention is "necessary or desirable". The Judge deliberately refrained from developing any "thresholds" which would fetter that discretion in any way, saying each case must be decided on its own facts.
- In determining whether to grant an order, the court must undertake an evaluative exercise. It is up to the Court to determine what matters to take into account but these should include an element of risk management or risk assessment.
- The FMA is not required to demonstrate prima facie liability but "must at least show that good grounds exist for the investigation and its continuation".
- Similarly, the FMA need not show that the assets are about to be dissipated, only that there is the potential for dissipation.
- The Court should consider the nature and seriousness of the breaches, the number of aggrieved persons and the quantum of the liability of the relevant person.
- Also relevant is whether the orders are sought by the FMA or by private interests. "Sprinkled through the Australian authorities is comment to the effect that the public interest role of the Authority may warrant an order in circumstances where it might be denied to a private litigant." However, the Courts should be careful not to attach too much weight to this factor as that would be tantamount to substituting the FMA's judgement for the Court's.
- Orders can only be made in respect of certain categories of property – i.e. assets held or controlled by the relevant person or money held by a third party on the relevant person's behalf. For interim orders, however, the Court need only be satisfied that it is "desirable" that an order be made without the FMA needing to prove that the property falls within the criteria specified in the legislation.
- Jurisdiction cannot be exercised for a disciplinary purpose but to preserve the status quo pending final judgment. Hence orders must be no more intrusive than required to preserve the assets.

Mr Hotchin's application to have the orders revoked was declined subject to an amendment to release the Hotchin family's "general household belongings". But the Judge revoked the orders against the two trusts because the evidence showed that they were genuinely independent and that his relationship with them was at arms' length.

"Powers of appointment of trustees, and even discretionary beneficiaries, are not sufficient to give Mr Hotchin control over the assets of the Trusts, because that control rests, at law, with the trustee once appointed," the Judge said.

The Judge also accepted that the investigation into the Hanover companies and Mr Hotchin had dragged on and advised the FMA that it must move "with all reasonable speed" and must provide progress reports to the Court within two weeks of the judgment (by 20 May) and via a telephone conference in June.

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