IN THE DISTRICT COURT
AT AUCKLAND

CRI-2009-004-028349

COMMERCE COMMISSION
Informant

v

BUDGET LOANS LIMITED
Defendant

Hearing: 26 July 2010

Appearances: C Paterson for the Informant
G Walker for the Defendant

Judgment: 26 July 2010

NOTES OF JUDGE D M WILSON QC ON SENTENCING (ORALLY)

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[1] Budget Loans Limited is a limited liability company. It is a wholly-owned subsidiary of Cynotech Finance Group Limited, which in turn is owned by Cynotech Holdings Limited.

[2] In November 2006 Cynotech Holdings Limited acquired the loan book of National Finance-2000 Limited for $7.7 million. Many of those loans were in arrears. The work that Budget Loans Limited does is in subprime lending. What happens is it lends to people who do not have access to money through first tier lenders, banks and the like. This means that the people with whom it deals are

generally less sophisticated, less aware and less able to protect themselves. The factor in the case, therefore, is victim vulnerability.

[3] There were originally some 110 individual informations, but when the case was called today on its first calling, counsel for the defendant company, Mr Walker, entered pleas of guilty to 34 informations and the prosecution withdrew the rest. These are charges that relate to breaches of the Fair Trading Act. They fall into four categories.

The welcome letters

[4] Those that are recognised by counsel for the informant, Ms Paterson, and also by Mr Walker as the most serious category of offending were what is being called in this case, the welcome letters. There were seven of these. The letters themselves were written to the debtors of the defendant company and in the course of the letters it was stated that the defendant had acquired the loan book. It invited debtors to contact the defendant about setting a loan agreement with them. $15 was charged per welcome letter to the loan on either 13 or 17 October 2006. Those debtors who did make contact and agreed to sign new contracts received disclosure statements. The initial unpaid balance of the loan, which would be enough to settle the debt, included the $15 letter fee. This amounts to a representation that the defendant had the right to charge the letter fee, but it did not have that right as is conceded. The failure to disclose the letter fee and its amount to the debtor meant that the defendant had no authorisation from the debtor for the charging of the fee and therefore had misrepresented its right to do so by including that in the initial unpaid balance.

[5] These letters and the charges that arose from them were done without (the defendant) obtaining legal advice. Counsel for the informant submitted that the welcome letter charges were imposed recklessly and without any right to do so. Counsel took a rather stern view of the way in which this was undertaken. Counsel suggested that a starting point in relation to those charges, of which there are seven, should be in the range of $35,000 to $42,000. Counsel relied on *R v Senate Finance Limited*[1]; an oral decision of Judge Callander given in the early days of prosecutions

[1] 14/11/06, Judge Callander, Auckland DC CRN 2006-450-2955.

of this type under the Credit Contracts and Consumer Finance Act 2003 in November 2006. In that case, disclosure requirements were not met because the contracts were sent out by facsimile and no one could read them. There was, therefore, no disclosure.

[6] Mr Walker submitted that it was unfair to criticise these actions as being "Grossly reckless". Certainly responsibility has been accepted, but he points out that the purchase of the loan book had taken place in November 2006. The loans were in arrears. He submitted that, generally speaking, the $15 would be regarded as a fairly modest establishment fee and that figure should be regarded as a contribution to the administrative costs. He says that such establishment fees are commonplace, even amongst first tier lenders. But the defendant here does submit that it was wrong to make the charges. On the evidence of the affidavit filed with these submissions, he points out that each of these charges has been reversed.

[7] I am inclined to accept the submission of Mr Walker, that the action of seeking recovery of this contribution to the cost of establishing the new loans following the failure of National Finance, should not be described as "grossly reckless". But to be fair to the submissions made by Ms Paterson, the action was taken without advice and during the setup of a significant enterprise like this, it should be expected that an operator like Budget Loans Limited would take advice.

[8] I agree with both counsel that the welcome letters charges are those that carry the greatest degree of culpability.

The lesser charges

[9] The rest of the charges relate to breaches which, in effect, amount to attempts to contract out of the legislative framework which overlies transactions of this kind, and in particular, the Credit (Repossession) Act 1997. When the contracts were taken over, the arrangements were that the defendant was granted a security interest in consumer goods, mostly motor vehicles.

[10] Clause 14 of the contracts purported to allow the charging of penalty interest on the out paying balance until full settlement of the loan contract, notwithstanding judgment against the debtor. Clause 14 amounted to a representation of a right by the defendant that it was entitled to make that claim, that is to allow the charging of penalty interest until the instalment had been paid by the debtor notwithstanding judgment against the debtor. This is in the face of s 35 of the specific provisions of the Credit (Repossession) Act 1997 which prohibits the charging of interest on a debt once the secured item has been seized and sold by the creditor. There is also an effect which is that clause 14 was, in effect, an attempt to contract out of the Credit (Repossession) Act 1997 in breach of s 42 of the Act. So that this can be seen in context, I set out clause 14 at this point.

> If you fail to pay any instalment or other money (including any amount for which payment has been accelerated) due on the due date or on demand as the case may be you shall pay to the lender default interest on the unpaid daily balance from the due date of such instalment or from the date of receipt or deemed receipt of demand for the money as the case may be until actual payment of the instalment or amount. All default interest shall continue to be payable after and notwithstanding judgment against you.

[11] Mr Walker submitted that the clause as set out was not sufficiently sophisticated to deal with the exceptional case where s 35 of the Credit (Repossession) Act 1997 stopped the interest running. The relevant part of s 35 of that Act provides as follows:

> If the net proceeds of sale [of securitised goods which have been repossessed] are less than the amount required to settle the agreement under s 31 as at the date of sale, the creditor is not entitled to recover more than the balance left to deducting those proceeds from that amount (whether under a judgment or otherwise)

[12] Mr Walker submitted that the provision in the clause would have been satisfactory if the words, "subject to s 35 of the Act had been added". He also made the point that had those words been added, the generality of customers who were dealing with the defendant company would not have understood the import of those words.

Legal advice taken by defendant

[13] It is acknowledged by the Commission that in proceeding in respect to that part of the case, and indeed the pre and post possession notices and settlement quotes and indeed the final Personal Property Securities Act 1999 matters, the defendant company had taken legal advice and acted consistently with that legal advice. This means that the 12 charges which relate to clause 14, the 13 charges which relate to the pre and post possession notes and the two charges which relate to the "All present and after-acquired property" clauses were entered upon by the defendant company on advice.

[14] The person from whom they took the advice was a Mr Liddell, an experienced solicitor who has practised in Credit Law for many years. He is a published author in that area, he has given regular seminars, some of them, in fact, in conjunction with the Ministry of Consumer Affairs and the Commerce Commission. He has co-authored a book on the Personal Property Securities Act 1999. Mr Liddell specifically advised the defendant company that it was entitled to charge interest until securitised goods had been repossessed and sold. Apparently, I am advised, that he maintains that view despite having considered the Commission's opinion to the contrary.

[15] Of course what has happened here is the defendant has admitted these charges, so at least implies that it accepts the Commission's view of these matters (which the Commission had conveyed to the defendant company) was to be preferred. Mr Walker makes the submission that having sought and acted on advice from the acknowledged expert, the defendant's conduct cannot be described as the informant would have it, as "reckless" or "grossly reckless".

[16] In relation to the charges under the pre and post possession notices that the defendant was entitled to repossess "All present and after-acquired property", including household goods, again, the defendant acted in accordance with Mr Liddell's advice. In those cases, the defendant held security over all present and

after-acquired property under s 44 of the Personal Property Securities Act 1999. That section provides:

> A security interest in after-acquired property attaches without specific appropriation by the debtor, unless the after-acquired property is consumer goods where –
>
> > (a) those consumer goods are not an accession or do not replace the collateral described in the security agreement; or
> >
> > (b) the security interest in those consumer goods is not a purchase money security interest.

[17] The legal result of that section is that the defendant had to appropriate the consumer goods falling within the exceptions provided by s 44(a) and 44(b) before repossessing them. Again, the defendant acted in accordance with Mr Liddell's advice: advice he still thinks it is correct. However, the defendant has modified its notices so that they now conform to the Commission's view of the legislation. There is no evidence that any consumer goods were repossessed in breach of the Act.

The informant's submissions on sentence

[18] Ms Paterson relies on the characterisation of the conduct of the defendant as reckless or grossly reckless to submit that an appropriate overall starting point for these offences would be in the range of $90,000 to $110,000. The informant acknowledges the steps that have been taken by the defendant, including the obtaining of legal advice and acknowledges that a significant discount should be available. She submits that given the objectives of the Act which are essentially consumer protection objectives, the importance of the untrue statements that were made is also a significant factor.

[19] There were three types of false representations and these, in many cases, were in fact acted upon by the defendant as if it had the right, which it asserted, when it did not have that right. She submitted that the culpability in terms of the representations were reckless, if not grossly reckless, and submits also that although the defendant obtained external and expert advice, that that characterisation of reckless or grossly reckless is still justified because the Commerce Commission's position was known in the industry and the defendant did not go to the Commission

to discuss those views or seek a second opinion. She points to the Commission specifically advising the defendant about its concerns regarding the practice of repossession by letter on 19 December 2007, 23 May 2008, 18 December 2008 and 29 April 2008. She points out that there was an interview on 13 June 2008 where the charging of letter fees was discussed.

[20] Ms Paterson relies also on what she describes as the complete departures from the truth in the sense that the defendant purported to have a right which it did not in fact have. The wide dissemination was a factor as well. Prejudice arises from debtors being charged fees and interest which they should not have been charged. The Commission's job is to deter breaches of the Act and call upon the Court to support it in that area.

[21] So she asks the Court to denounce the behaviour, deter the defendant and others from the conduct and to deal consistently with other authorities. The informant submits that the defendant should be held accountable because consumer protection legislation aimed at protecting the rights of consumers and preventing misleading and deceptive conduct are principles which need to be upheld.

The authorities

[22] She cites the decision of Judge Callander at paragraph 17 in *R v Senate Finance Limited*[2] where His Honour said:

> The purpose of both Acts (the CCCF Act and the FTA) is self-evident. It is to protect the interests of consumers entering into credit contracts, provide for the disclosure of adequate information to those consumers and prevent misleading and deceptive conduct, false representations and unfair practices. Consumer rights, the disclosure of information developed over the last few decades prescribe that anything that is material in a contractual relationship between vendor and purchaser or a shopkeeper and consumer must be made clear and conspicuous in the interests of fairness and honest trading. Those concepts underpin both pieces of legislation.

[23] Of course that was a case where the detailed terms of the contracts could not be read because they were faxed out. This informant also refers to the need to

[2] 14/11/06, Judge Callander, Auckland DC CRN 2006-450-2955.

provide for interests of the victims of the offence. She says that the gravity of the offending can be measured, because the overcharge amounted to $500,386.01.

[24] Both counsel have referred to a number of cases. None of those cases are exactly the same as this. In *Commerce Commission v Marchione*[3]. Judge Bouchier was dealing with purported sales of motor vehicles by competitive tender auction processes. Once the sale had gone through, there was a deliberate arrangement under which employees of the defendant company would have people sign up to documents which purported to cancel out of the Fair Trading Act and the Consumer Guarantees Act 1993. Judge Bouchier held that that conduct was deliberate, designed to deceive members of the public, and that the statements were completely false. There had been wide dissemination of the representations, the defendant had been uncooperative and shown no remorse. A starting point of $1500 on each of the 32 charges was adopted and a fine of $48,000 was imposed.

[25] Even the prosecutor acknowledges that those more serious charges are more serious than the present. They were deliberate and premeditated and that as opposed to nearly as the prosecutor would have it, reckless. Counsel also referred to *Commerce Commission v Baker and Dolbel*[4]. In that instance there had been 22 representative charges and fines of $100,000 were imposed. The charges involved 10 representative charges under s 17 of the Credit Contracts and Consumer Finance Act 2003. Ten representative charges under s 17 and s 10 under s 25 of that Act. One representative charge under s 38 and one representative charge pursuant to s 13(1) of the Fair Trading Act. That, in fact, led to agreed fines being reached which do not, in my view, and with respect, are of limited value as precedent.

[26] In *Commerce Commission v Galistair Enterprises Limited*[5]. Judge Aitken was dealing with pleas of guilty to 98 representative charges under the Credit Contracts and Consumer Finance Act 2003 and one under the Fair Trading Act. The fine there was $45,000. That was a case involving security for loans being secured over cars. In that case it had written asking for advice about whether their arrangements complied with the law under the Credit Contracts and Consumer

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[3] 19/7/06, Judge Bouchier, Auckland DC CRN 2004-004-21773.
[4] Decision of Judge Aitken, 21 May 2007.

Finance Act 2003 and continued to use the old and non-complying forms in the meantime.

[27] It was a small company with something under half of its pre-tax profit coming from motor vehicle lending, which was what was the subject matter. A starting point was taken there of $70,000. There was discount made for a guilty plea and the repayment of excessive interest which amounted to just short of $24,000. Galistair was fined $45,000.

Defence submissions

[28] I agree with Mr Walker's submission that the actions of the defendant, the letters apart, cannot be characterised as "grossly reckless". The defendant had taken a responsible approach by seeking specialist legal advice. It tried to ensure that it was acting in full compliance with the relevant legislation. The distinction must be made with *Galistair*, where the starting point was $70,000 where *Galistair* proceeded without any legal advice. I think his point is a sound one, that in the case of Budget Loans Limited, they sought advice from a recognised expert and received advice that it was acting in accordance with its legal responsibilities.

[29] Indeed, also since this matter came to light, the defendant has undertaken to make cash refunds totalling $86,513.42. That is the actual amount that had been overpaid by people rather than the figure of over $500,000. Those were overcharges which were not paid and have been subsequently reversed. In addition to that, the defendant company has reordered its arrangements so that it complies with what it accepts to be the Commission's view of its legal obligations. It has, therefore, taken a significant number of genuine steps to put right what has been done that was wrong. For that, it deserves significant credit.

Discussion

[30] The result is that all that could have been done by way of reparation and amelioration has been done. The conduct of the defendant, once these matters came

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[5] 6/12/07, Judge Aitken, Auckland DC CRI 2007-004-004009.

to light, has been such that it has remodelled its arrangements. It is now compliant, it has made good voluntarily. It has pleaded guilty on the first appearance in Court.

[31] The prosecutor submitted that an overall fine in the region of $90,000 to $100,000 subject to a very significant discount in the range of 40 to 50 percent to reflect the admitted and asserted mitigating factors would be appropriate. This would lead, on a 50 percent reduction, to an end fine in the range of $45,000 to $50,000.

Result

[32] The greatest degree of culpability, as is accepted, applies to the seven welcome letters. In my view, an appropriate starting point there, bearing in mind that the maximum penalty for each breach is $200,000 would be a figure of $3000. In my view, and having regard to the decisions that I have referred to, the other 27 charges should not attract a greater starting point than $1500. The overall figure is one of $61,500 against which it is appropriate to allow a discount recognising the guilty pleas and the other mitigating factors of 50 percent. The overall fine, accordingly, should be $30,750.

[33] There is no application for solicitor's fees.

D M Wilson QC
District Court Judge