

SOUTHERN CROSS FINANCE LIMITED

COMMERCE COMMISSION

DEED OF SETTLEMENT

DATED

6 July

2010

DEED DATED

day of

2010

PARTIES

SOUTHERN CROSS FINANCE LIMITED ("SCFL"), 2/65 Mellons Bay Road, Howick, Auckland

COMMERCE COMMISSION ("the Commission") a statutory body established under section 8 of the Commerce Act 1986

BACKGROUND

- A. SCFL is a New Zealand-based, non-bank mortgage provider. It is beneficially and legally owned by a number of private parties.
- B. SCFL is required to comply with the Credit Contracts and Consumer Finance Act 2003 ("the CCCF Act").
- C. Section 41 of the CCCF Act states that a consumer credit contract must not provide for a credit fee or a default fee that is unreasonable.
- D. The term "credit fee" is defined in section 5 of the CCCF Act as, relevantly, a fee payable by the debtor under a credit contract, or payable by the debtor to, or for the benefit of, the creditor in connection with a credit contract.

- E. The loan establishment fee charged by SCFL falls within the definition of a credit fee, as do the loan renewal and loan extension fees charged by SCFL.
- F. Section 42 of the CCCF Act deals specifically with establishment fees, and sets out mandatory considerations for the Court in determining whether an establishment fee is unreasonable.
- G. Pursuant to section 42, establishment fees charged should be less than or equal to the creditor's reasonable costs of establishment, or the creditor's average reasonable costs of establishment for the relevant class of consumer credit contract.
- H. Establishment costs are specified in section 42 as costs associated with:
- The application for credit; and
 - Processing and considering that application; and
 - Documenting the consumer credit contract; and
 - Advancing the credit.
- I. Prior to the commencement of the CCCF Act, SCFL charged establishment fees which were generally set at 1% to 2% of the loan advanced.
- J. At the time that the CCCF Act came into force, SCFL took legal advice in respect of its obligations. The advice it received was that the establishment fees charged by SCFL (being 1% to 2% of the loan advanced) would not breach the CCCF Act.

- K. The Commission is of the view that establishment fees which are a percentage of the loan advanced are inherently unlikely to reflect the actual costs of establishment. This view was set out in a Commission booklet "Credit Contracts and Consumer Finance Act – A General Guide for the Credit Industry" published in March 2005.
- L. In 2009 the Commission requested SCFL justify the establishment fees it had charged on a number of consumer credit contracts.
- M. SCFL was unable to justify the fees referred to on a cost basis. It was unable to show that the establishment fees it charged were equal to or less than its actual reasonable costs of establishment, or its average reasonable costs of establishment for the relevant class of consumer credit contract.
- N. In October 2009 SCFL calculated that its average reasonable cost of establishing a consumer credit contract after 1 April 2007 was approximately \$1,260. It ceased charging establishment fees based on a percentage of the loan advanced, and now charges an establishment fee of \$500 on consumer credit contracts.
- O. After further analysis, SCFL calculated that its average reasonable cost of establishing a consumer credit contract prior to 31 March 2007 was approximately \$970.

- P. SCFL also charges its customers loan extension or renewal fees where loans are extended or renewed. SCFL and the Commission agree that these fees are also establishment fees as the renewal or extension relates to the creation of a new credit contract.
- Q. SCFL has calculated that its average reasonable cost of renewing or extending a consumer credit contract was approximately \$900 prior to 31 March 2007 and \$1,010 after 1 April 2007.
- R. SCFL acknowledges that it has charged unreasonable establishment fees on those consumer credit contracts established since 1 April 2005, where the fee charged was greater than the average reasonable fee (as set out above).
- S. SCFL has agreed to make refunds to debtors who entered into consumer credit contracts after 1 July 2006 and who were charged unreasonable establishment fees.

TERMS OF THIS DEED

1 PURPOSE

- 1.1 The purpose of this Deed of Settlement ("Deed") is to:
- (a) document a settlement between the parties in relation to the Commission's investigation of the establishment fees charged by SCFL ("the Investigation"); and

- (b) provide a mechanism for refunding debtors who were charged unreasonable establishment fees between 1 July 2006 and October 2009 ("Affected Debtors").

2 AGREEMENT

- 2.1 SCFL acknowledges and admits the facts referred to in paragraphs A to S (inclusive) of the Background above.
- 2.2 SCFL admits and agrees that it has charged unreasonable establishment fees on consumer credit contracts and thereby breached section 41 of the CCCF Act.
- 2.3 SCFL agrees to refund the amounts it has overcharged debtors who entered into consumer credit contracts and who were charged unreasonable establishment fees during the period 1 July 2006 to 31 October 2009.
- 2.4 The Commission agrees that it will cease the Investigation, subject to clause 10.3 of this Deed.

3 DETERMINATION OF CONSUMER CREDIT CONTRACTS

- 3.1 The definition of a consumer credit contract is set out in section 11 of the CCCF Act. Sections 14 and 15 are also relevant.

3.2 In summary, a credit contract is a consumer credit contract if:

- (a) the debtor is a natural person (therefore, loans to companies and to trusts - including family trusts - are not consumer credit contracts); and
- (b) the debtor enters into the contract primarily for personal, domestic, or household purposes (therefore, loans for business or investment purposes are not consumer credit contracts).

3.3 The CCCF Act does not define "primarily" or "personal, domestic or household purposes" and there has not been judicial consideration of these phrases.

3.4 For the purposes of this Deed and settlement the Commission and SCFL have agreed that the following principles will be applied in determining whether a loan is a consumer credit contract and falls within the scope of this Deed.

- (a) Where 50% or more of the credit is applied for domestic purposes the loan will be a consumer credit contract. This approach is consistent with that taken in Australia.
- (b) Where credit is taken out for the benefit of family members (including parents, children and siblings) and used by those persons for their domestic purposes, the loan will be a consumer credit contract. This is consistent with Australian case law.

- (c) For clarity, applications made in order that a person can further a business arrangement or give effect to a business purpose, but which require and incorporate the refinancing of a personal loan, will be a consumer credit contract where the condition set out in (a) above is met.

3.5 For the purposes of this Deed, the Commission shall be the final arbiter on whether a credit contract is a consumer credit contract and therefore subject to this Deed.

4 CALCULATION OF REFUNDS PAYABLE TO CUSTOMERS

4.1 SCFL has calculated a "reasonable" establishment fee, being its approximate average cost of establishing a consumer credit contract as follows:

- Prior to 1 April 2007 - \$968.43
- From 1 April 2007 - \$1,257.56

4.2 SCFL has calculated a "reasonable" loan extension or renewal fee, being its approximate average cost of renewing or extending a consumer credit contract as follows:

- Prior to 1 April 2007 - \$898.43
- From 1 April 2007 - \$1,009.56

4.3 The refund shall be:

- the amount of the establishment fee (or renewal or extension fee) charged less the "reasonable" fee; plus
- the interest that has been charged by SCFL on the "overcharged" portion of the fee.

4.4 For the sake of clarity, we set out an example of the calculation. Where:

- the "reasonable" establishment fee was \$1,257.56; and
- the establishment fee charged by SCFL was \$5,000; and
- the loan was for 6 months with interest charged at 12% per annum.

The amount of the refund would be \$3,966.99, being \$3,742.44 ($\$5,000 - \$1,257.56$) + \$224.55 ($\$3,742.44 \times 12\% \times 6/12$).

4.5 SCFL has made a preliminary estimate of the total refunds payable. Total refunds are expected to be \$690,000, comprising fee refunds of \$602,000 and refunds of interest on those fees of \$88,000. There are 253 affected loans.

5 REFUND PROCESS

Payment Constraints and Timing

- 5.1 SCFL currently receives its funding from BOS International (Australia) Limited ('BOS'). BOS imposes certain constraints on SCFL and requires that SCFL maintain specified levels of profitability and equity.
- 5.2 SCFL has advised the Commission that these constraints mean that its capacity to make refunds is limited to \$35,000 per month.
- 5.3 SCFL therefore agrees to make provision for refunds of \$35,000 per month commencing June 2010 until such time as all refunds have been paid (whether to the debtor or in accordance with the Unclaimed Monies Act 1971).
- 5.4 It is estimated that the total amount to be refunded is \$690,000, of which approximately \$162,000 relates to loans where there was a shortfall on repayment and accordingly refunds are not required to be repaid to the debtors in cash. It is expected that the remaining refunds amounting to approx \$528K (including interest refunds) will take approximately 16 months to be paid.

Outline of Refund Process

- 5.5 Refunds will be paid in the following order:

- (a) Affected Debtors who hold active loan accounts with SCFL will have their accounts credited with their refunds. It is estimated that refunds of approximately \$133,000 are payable to 48 debtors. Taking into consideration SCFL's funding constraints, refunds to this group of debtors are to be completed prior to 30 September 2010. SCFL shall determine the appropriate allocation of the refund amount each month.
- (b) Next, all Affected Debtors with closed loan accounts who are to be refunded \$1,200 or less will be refunded in full. It is estimated that this will be approximately 78 debtors with refunds totalling approximately \$37,000. These payments will be made in October 2010.
- (c) Next, all Affected Debtors with closed loan accounts who are to be refunded between \$1,200 and \$1,850 will be refunded in full. It is estimated that these refunds will approximate \$35,000 and relate to approximately 23 debtors. These payments will be made in November 2010.
- (d) From 1 December 2010, the sum of \$35,000 will be repaid monthly to the remaining Affected Debtors whose accounts have been closed. The amount payable to each debtor each month will be a pro-rata share of the refund payable.

- 5.6 In the case of Affected Debtors who had loan accounts with SCFL and whose loan balance has been written-off by SCFL because of non-payment, SCFL will credit the refund to the debtor's account (as per clause 5.4 above). This accounting exercise must be completed by 30 September 2010. Should the amount refunded exceed the written-off balance, the debtor will be entitled to refunds along with the other closed accounts referred to in paragraph 5.5.

Notice to Affected Debtors

- 5.7 The procedure for contacting Affected Debtors entitled to a refund and providing them with notice of the refund shall be:
- (a) Within ten working days of the execution of this Deed, SCFL will submit to the Commission for its approval draft letters to all Affected Debtors. The letters will include those matters set out in clause 6.1 of this Deed.
 - (b) As soon as practicable, and no later than five working days after receipt of the Commission's written approval of the draft letters, SCFL will write to the Affected Debtors specified in paragraph 5.5(a), at their last known address in the form of the approved letter.
 - (c) By 30 September 2010 SCFL will write to the Affected Debtors specified in paragraph 5.5(b), at their last known address in the form of the approved letter advising them of their refund.

- (d) By 31 October 2010 SCFL will write to the Affected Debtors specified in paragraph 5.5(c) at their last known address in the form of the approved letter advising them of their refund.
- (e) By 30 November 2010 SCFL will write to the Affected Debtors specified in paragraph 5.5(d) at their last known address in the form of the approved letter advising them of their refund.

Form of Refund

- 5.8 SCFL will make the refund to debtors with closed accounts in the appropriate month as specified in paragraph 5.5 on receipt of either New Zealand bank account details or confirmation of a current mailing address details. Where the Affected Debtor has an existing New Zealand bank account, SCFL will arrange for payment of the refund by direct credit to that debtor. Alternatively, on request by the debtor, SCFL will arrange for the refund to be paid by cheque.
- 5.9 In the event of no initial response from any Affected Debtor, SCFL will undertake the further steps set out in the document entitled "Refund Process" attached hereto and marked as Schedule A in an effort to make payment.

5.10 If a debtor has not been located after the steps taken in the "Refund Process" attached hereto as Schedule A have been completed, or a cheque is returned to SCFL or is not presented within six months of its issuance, then SCFL will account for those monies in accordance with the Unclaimed Monies Act 1971.

6 NOTICE REQUIREMENT

6.1 All notice or letter templates required to be given under this Deed shall not be sent or published unless approved by the Commission (such approval not to be unreasonably delayed or withheld). All notices or letters shall contain at least the following terms:

- (a) An acknowledgement that SCFL has reached a settlement with the Commission in relation to unreasonable establishment fees charged on consumer credit contracts;
- (b) An admission that SCFL has breached the CCCF Act;
- (c) Details of the refund including:
 - (i) the basis upon which the refund has been calculated; and,
 - (ii) the terms upon which the refund will be paid; and,

- (iii) the amount that is to be refunded to the debtor.
- (d) That the debtor is not bound to accept the refund offered to them, and that they may take their own private action against SCFL if they believe that the refund does not fully compensate them for their loss.
- (e) That the debtor should contact SCFL directly with their New Zealand bank account details, or a current mailing address if they wish to receive their refund by cheque.
- (f) Details of a telephone number and email address that the debtor may use to contact SCFL if they have any queries about the refund.
- (g) That if the debtor does not respond or otherwise wish to accept the refund, SCFL may, having followed the steps set out in Schedule A and being unable to locate the debtor or make payment to their bank account, account for the refund in accordance with the Unclaimed Monies Act 1971.

7 REPORT REQUIREMENT

- 7.1 SCFL shall provide an Initial Report to the Commission of the refund process as set out in this Deed. The Initial Report shall specify the date and the amount of the refunds made to debtors with active accounts.

- 7.2 The Initial Report shall be provided by 21 October 2010.
- 7.3 Further Reports, specifying the date and the amount of the refunds made to debtors in and including full details of efforts made to locate debtors who have not been refunded are required by 21 December 2010, and every six months thereafter until refunds have been made to all debtors in full.

8 SCFL FUNDING ARRANGEMENTS

- 8.1 SCFL's funding facility from BOS has a final expiry date of 23 August 2011. SCFL is currently investigating funding options.
- 8.2 SCFL will inform the Commission of its new funding arrangements, when these are confirmed.
- 8.3 Should no new funding arrangements be made, SCFL will continue the fee repayment programme of \$35,000 per month as documented in this Deed.
- 8.4 If SCFL should sell or transfer over 50% of its loan book to another entity, or be placed in receivership or liquidation, the full amount of the refund outstanding to debtors is immediately due and payable by SCFL.

9 REVIEW REQUIREMENT

- 9.1 SCFL agrees that the Commission may conduct a review of the refund process to ensure that it has been conducted in accordance with the terms of this Deed.
- 9.2 If the Commission so requests, SCFL shall, at its own cost, engage an independent reviewer approved by the Commission to review the refund process set out in this Deed.
- 9.3 The independent reviewer shall verify and provide a comment on the process and/or any of the Reports to be provided by SCFL to the Commission as described in clause 8 above and provide an opinion on whether the refund process has been satisfactorily completed in accordance with the terms of this Deed.

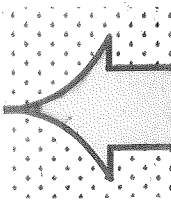
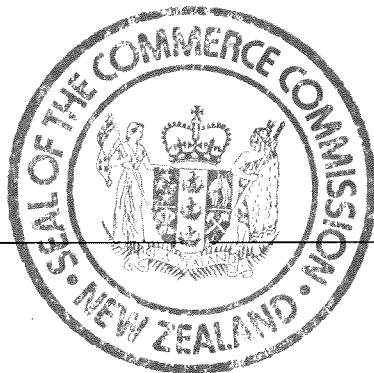
10 IMPLEMENTATION AND EFFECT OF THE DEED

- 10.1 This Deed does not preclude any person who has not consented to be bound by the terms of this settlement from taking action against SCFL under the CCCF Act. The Commission agrees to be bound by this Deed and to discontinue its current Investigation and not bring any further or other action in relation to the matters referred to in paragraphs A to S (inclusive) of the Background above, subject to clause 10.3 of this Deed.

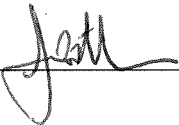
- 10.2 Either party may publish the facts of this investigation and settlement and may subsequently refer to them. This may include publicity by press statements, articles, publications or speeches prepared or given by Commission members or staff.
- 10.3 If there is any material breach of SCFL's obligations under this Deed (other than where that breach is due to undue delays by the Commission in responding to any request for approval or is caused by matters outside the control of SCFL), the Commission may in its complete discretion recommence the Investigation and take any action it deems appropriate including commencing civil proceedings, prosecution under the Fair Trading Act 1986, the Commerce Act 1986 and/or the CCCF Act.
- 10.4 If the Commission commences any Court proceedings pursuant to clause 10.3 above, SCFL hereby waives any limitation defence that may be available to it in respect of those proceedings to the extent that limitation defence arose solely as a result of the settlement recorded in this Deed.

EXECUTED by and under the name and seal of **THE COMMERCE COMMISSION** by:

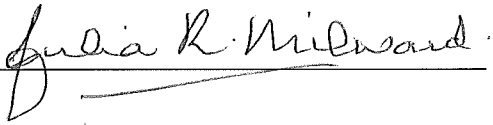
Anneke Reilly



EXECUTED by **SOUTHERN CROSS FINANCE LIMITED** by



Director



Director

SCHEDULE A: REFUND PROCESS

Step 1

Mail a letter to Customer (at the last address on file) advising of the refund amount due and requesting customer to contact SCFL.

Step 2

If Customer makes contact, refund money via direct credit (or cheque if requested).

Step 3

If Customer has not made contact after 10 working days, telephone customer to advise them of the refund (try all phone numbers on file), and request account details for refund.

If no response -

Step 4

Search electronic White Pages to locate new address and telephone number. Contact next of kin or other contacts on file (eg.solicitor, broker) to locate new address and/or telephone number.

Attempt to make contact to arrange refund.

If no contact has been made and the amount outstanding is greater than \$500 -

Step 5

Search electoral rolls and/or conduct google searches to attempt to locate Customer.

Send letter as at Step 1

If no contact has been made after Step 4 (for refunds less than \$500) or Step 5 (for refunds greater than \$500) -

Step 6

Classify as Gone No Address.

Maintain a spreadsheet with details of Customers not contacted (including details of customer, refund due, and all attempts made to contact Customer). Inform the Commerce Commission investigator of Customers not contacted and attempts made to contact those Customers.