IN THE DISTRICT COURT
AT AUCKLAND

CRI-2016-004-005745
[2016] NZDC 19377

THE QUEEN

v

SMART SHOP LIMITED

Hearing:	30 September 2016
Appearances:	S Lowery for the Crown G Carter for the Defendant
Judgment:	30 September 2016

NOTES OF JUDGE R G RONAYNE ON SENTENCING

Introduction

[1] Smart Shop Limited has pleaded guilty by notice pursuant to the procedure in s 38 Criminal Procedure Act 2011.

[2] I group the charges together in the same way as set out on the first page of the caption summary.

[3] The first group is that it made false or misleading representations concerning the existence, exclusion or effect of any condition warranty, guarantee, right or remedy including to avoid doubt in relation to any guarantee, right or remedy available under the Consumer Guarantees Act 1993. There are three such charges, CR numbers ending 2884, 2885 and 2886. Those charges relate to breaches of s 13 and s 40 of the Fair Trading Act 1986 and carry maximum penalties each of $600,000.

[4] The second group of three charges (CR numbers ending 2878, 2879 and 2880) charge that the company, being a creditor under a consumer credit contract, failed to disclose key information applicable to the contract to the debtor in breach of sections 17 and 103 (to 5 June 2015) and 102A (from 6 June 2015) of the Credit Contract and Consumer Finance Act 2003 ("CCCFA"). Those charges attract a maximum penalty of $30,000.

[5] The third group of three charges (CR numbers ending 2881, 2882 and 2883) charge that the company, being a creditor under a consumer credit contract, failed to provide disclosure applicable to an agreed change to the contract to the debtor in breach of sections 22(1)(a) and 102A CCCFA. Those also attract a maximum penalty of a fine of $30,000.

[6] The fourth group of two charges (CR numbers ending 2887 and 2888) charge that the defendant, being a warrantor under an extended warranty agreement, failed to disclose to consumers the required information about the agreement, in breach of sections 36U and 40(1B) Fair Trading Act 1986 ("FTA"), again attracting a maximum penalty of a fine of $30,000.

The facts

[7] The defendant, Smart Shop Limited, traded as Smartstore and was incorporated on 30 May 2012.

[8] SmartStore is part of the "Shop Direct" group of companies, together with other entities operating under the trading names of "Shop Direct" and "Gadgets+" and share resources, including office premises, staff and office systems. The group of companies operate as mobile traders. Mobile traders, also known as "truck shops", are businesses that do not have fixed retail premises in the traditional sense. Some of these traders operate mobile shops, usually from trucks, while others employ sales staff who sell goods door to door using catalogues and brochures. The "Shop Direct" group sells door to door using catalogues and brochures.

[9] SmartStore sells electronic goods direct to consumers, using a combination of "door Knocking" and telemarketing. Those consumers are often unable to obtain credit from established retail outlets to purchase electronic goods. Salespeople "door knock" for new customers and make repeat sales to existing customers by telemarketing. SmartStore has advised that the salespeople are paid solely on commission.

[10] The electronic goods are sold to consumers at prices that are much higher than their normal retail price. For example, a Konka 40" TV was sold by SmartStore for $2000 instead of the usual retail price of $549 and a Samsung Galaxy S4 smartphone was sold by SmartStore for $1800, instead of its usual retail price of around $400. When a consumer purchases a SmartStore product, he or she does so by entering into a "Fixed Instalment Credit Contract" ("Credit Contract"), whereby the purchase price is repaid by the consumer over a number of weekly instalments. A number of other fees are also payable under the Credit Contract, detailed below. When the consumer's account balance fell below a certain level, SmartStore's telemarketers would contact the consumer to sell more electronic goods.

[11] SmartStore also offer consumers, who purchase electronic goods, membership in the "Smart Club", for an additional $5 per week. Membership offered consumers a number of additional benefits, detailed below.

[12] In recent years, the business practices of mobile traders have become more prominent in the complaints the Commission has received from consumers and their advocates.

[13] Shop Direct Lifestyle Limited was investigated on 7 May 2014 given advice about complying with its disclosure requirements under the CCCFA. The Commission also raised concerns that the company was at risk of making representations that purported to contract out of the Consumer Guarantees Act 1993 ("CGA").

[14] In June 2014, the Commission opened an investigation into the mobile trader industry with a view to changing industry behaviour. The Commission identified 32

mobile traders who operated throughout New Zealand. The majority were based in the North Island, with a particular concentration in Auckland.

[15] Most mobile traders were issued with compliance advice on their contracts by the Commission. On 25 February 2015 SmartStore, Shop Direct and Gadgets+ were each issued with advice about complying with the disclosure requirements in the CCCFA and the uninvited direct sales provisions of the FTA.

[16] In August 2015, the Commission published its report on the mobile trader industry, highlighting systemic compliance issues with respect to traders' obligations under the CCCFA, in particular the requirement to provide adequate disclosure to consumers prior to entering into consumer credit contracts. There was significant media publicity over the report and its findings, and the Commission made mobile traders aware of the report.

[17] The extended warranties provisions in Subpart 3 of Part 4A of the FTA were introduced on 17 June 2014. The Commission initially took an educational approach by contacting businesses offering extended warranties and advising them of the existence of the new provisions. The Commission contacted the "Shop Direct" group of companies about the Smart Club membership on 17 March 2015.

[18] The investigation regarding the present matters began when the Commission became aware that the Shop Direct Group was continuing to provide extended warranties in the form of club memberships. The investigation was ultimately broadened to include the other alleged breaches of the CCCFA and FTA in relation to the Credit Contracts.

[19] SmartStore entered into 2415 Credit Contracts with debtors between 25 February and 31 October 2015. As many as 1209 debtors also purchased a SmartClub membership during that period. It is unclear how many of the 1209 SmartClub memberships were active during the charge period.

[20] The standard form documentation provided to debtors consisted of the Credit Contract document, a "SmartClub membership" document, and a "Credit Contract

Disclosure" statement. That documentation was in breach of the CCCFA and FTA because:

(a) The Credit Contract failed to disclose key information applicable to the contract to the debtor, in breach of s 17 CCCFA;

(b) False or misleading representations were made in the Credit Contract about the existence or exclusion of the debtor's rights or remedies under the CGA, in breach of s 13(i) FTA; and

(c) The SmartClub membership failed to disclose information about the extended warranty agreement and the CGA, as required by s 36U of the FTA.

[21] SmartStore has subsequently advised the Commission that it had 102 active Credit Contracts that have been varied by agreement between Smart Store and the debtor. The Commission reviewed three of those Credit Contracts and found that Smart Store failed to provide the disclosure in respect of those variations, as required by s 22(1)(a) of the CCCFA.

[22] Each of these breaches is addressed in turn below.

Failure to disclose key information – s 17 CCCFA

[23] Debtors entered into the Credit Contracts with SmartStore for the purchase of electronic goods. The goods were delivered to the debtor after a minimum number of instalment payments, and the remainder of the purchase price is paid off through weekly instalments. The debtor is charged fees under the Credit Contract:

(a) A delivery fee each time a delivery is made (of between $25 and $30);

(b) An establishment fee of $75 at the time of opening the account;

(c) A monthly account fee of $5 for account maintenance when the balance is unpaid (which will almost always be the case); and

(d) a dishonour fee of $15 per failed direct debit payment.

[24] The Credit Contract and Credit Contract Disclosure documents did not disclose to the debtor key information applicable to the contract as set out in Schedule 1 of the CCCFA. Nor was sufficient disclosure provided to the debtor at a later date. Specifically, SmartStore failed to disclose:

(a) A statement of the debtor's right to cancel the contract in compliance with s 27 CCCFA. While the Credit Contract referred to the debtor's right to cancel "within five (5) days", the actual wording of the CCCFA gave debtors three working days (to 5 June 2015) or five workings days (from 6 June 2015) to cancel from the day that disclosure was made. The Credit Contract also failed to advise the debtor that he or she had the right to pay the cash price of the goods on cancellation, and required the debtor to return the various forms and notices given to him or her at the time the contract was entered into;

(b) That the initial unpaid balance also included credit fees such as an establishment fee, delivery fee and monthly administration fee. The definition of "Initial Unpaid Balance" in the Credit Contract Disclosure document referred only to the total purchases made as at the date of the original contract, but all Credit Contracts also incurred an establishment fee and delivery fee, and monthly account fees of $5;

(c) That the total of all advances made or to be made in connection with the Credit Contract included the monthly account fee and, if applicable, the Smart Club membership fee. The "TOTAL contract price" on the Credit Contract did not include the monthly account fee, which was loaded against the debtor's account. It also did not take into account the weekly Smart Club membership fee, which was also debited against the debtor's account;

(d) The total amount of payments to be made to repay all advances in connection with the Credit Contract. While the Credit Contract contained a box where the SmartStore representative could write in the total number of weekly payments, this figure was inadequate to completely repay all advances because it did not take into account the monthly account fee and, if applicable, the Smart Club membership fee;

(e) (From 6 June 2015) the debtor's right to apply for relief on grounds of unforeseen hardship under s 55 CCCFA, and advice on how such an application may be made; and

(f) (From 6 June 2015) the frequency with which continuing disclosure statements would be provided. Following an amendment of the CCCFA, from 6 June 2015 creditors were required to provide debtors with continuing disclosure statements, even where the amount of each advance is known to the debtor and payments are to be made in accordance with a specified schedule.

Failure to provide disclosure in relation to agreed variations – s 22(1)(a) CCCFA

[25] These charges relate to three specific variation agreements that the Commission has reviewed. The variation agreements were entered into with Nicholas Karetu on 31 July 2015, Philippa Taitai on 31 August 2015, and Atinta Tiaon on 28 October 2015.

[26] In each instance SmartStore and the debtor agreed to vary their credit contract, by extending a further advance to the debtor in connection with the purchase of additional electronic goods. SmartStore failed to provide those debtors with the required disclosure in relation to the variation, pursuant to s 22(1)(a) CCCFA.

[27] Instead, the debtors were given a document entitled "Variation Disclosure" that recorded the newly purchased item and its cost, but failed to disclose:

(a) A statement of the debtor's right to cancel the Credit Contract in compliance with s 27 CCCFA. While the Variation Disclosure referred to the debtor's right to cancel with "five (5) days", this did not comply with the actual wording of the CCCFA. The Credit Contract also failed to advise the debtor that he or she had the right to pay the cash price of the goods on cancellation;

(b) (In respect of the Karetu and Taitai variations) the total unpaid balance under the contract, including the outstanding balance prior to the new purchase, the new outstanding balance and the monthly administration fee;

(c) (In respect of the Karetu and Taitai variations) that the total of all advances made or to be made in connection with the contract included the monthly account fee and the Smart Club membership fee;

(d) The total amount of payments to be made to repay all advances in connection with the Credit Contract. While the Variation Disclosure document said "please now pay: x weekly payments of $y", in respect of Mr Karetu and Ms Taitai, it was inadequate to completely repay all advances because it did not take into account the monthly account fee and the Smart Club membership fee. In respect of Ms Tiaon, the number of weekly payments specified was significantly in excess of what was required to repay all advances;

(e) That the debtor had the right to apply for relief on grounds of unforeseen hardship under s 55 CCCFA, and advice on how such an application may be made; and

(f) The frequency with which continuing disclosure statements would be provided.

False or misleading representation concerning the existence, exclusion, or effect of any condition, warranty, guarantee, right or remedy – s 13(i) FTA

[28] The Credit Contract Disclosure document sets out the terms and conditions applicable to the Credit Contracts and contained 26 clauses. A number of those clauses misrepresented the debtor's rights under the CGA. Section 43(1) of the CGA provides that the provisions of the CGA shall have effect notwithstanding any provision to the contrary in any agreement.

[29] Clause 8 of the Credit Contract Disclosure document stated:

> **8 Consumer Guarantees**
>
> 8.1 Where the Consumer Guarantees Act 1933 applies, you shall have all the rights and remedies provided under this Act but no others.

That general clause was insufficient to correct the specific clauses that followed which conflicted with the debtor's rights under the CGA. A debtor reading the Credit Contract Disclosure document would not have been aware of the rights and remedies provided to him or her by the CGA, or that where the specific clauses of the document conflicted with the provisions of the CGA, the latter would apply.

[30] The specific clauses that misrepresented the debtor's rights or remedies under the CGA were:

(a) Clause 12 stated that SmartStore made "no warranties or representation and expressly negates any implied or express condition that the goods will be suitable for a particular purpose or use for which you may use them". In fact, ss 6 and 7(1)(a) of the CGA guarantee that goods are of an acceptable quality, which includes that they are fit for all the purposes for which goods of the type in question are commonly supplied;

(b) Clause 13 required the debtor to notify SmartStore within two working days of delivery of the goods if the goods were of unacceptable quality. In contrast, s 20 of the CGA actually entitles

consumers to reject goods within a reasonable time from the time of supply;

(c) Clause 14 stated that SmartStore has the option of requiring the debtor to return rejected goods, and then SmartStore is able to elect to repair or replace the goods, or refunding the purchase price if already paid. In fact, s 23 CGA provides that where the consumer rejects goods, he or she is able to choose a refund or to have the goods replaced; and

(d) Clause 20.1(a) stated that delivery of the goods to a carrier by SmartStore is deemed to be delivery of the goods to the consumer. In fact, ss 5A and 20(1)(b) of the CGA provide that a carrier of goods is an agent of the supplier, therefore delivery to the consumer is not effected until the consumer receives the goods.

Failure to provide the required information about an extended warranty agreement – s 36U FTA

[31] The Smart Club membership was sold to debtors at the time that they agreed to purchase the electronic goods, for an additional $5 per week. The Smart Club membership form initially contained 10 clauses under the "Terms & Conditions" section. Clause 2 specified:

> While you are a member of Smart Club, we will extend the term of the Manufacturer's Warranty by 12 months (to a maximum of 36 months). This in no way effects your rights under the Consumer Guarantees Act 1993.

[32] Clause 2 was removed from the membership form in a later version. Smart Club continued to offer to its members, however, a number of specific warranties, guarantees or undertakings in relation to the goods, namely:

(a) Where goods are covered by the manufacturer's warranty, a guarantee that goods would be repaired within 48 hours (weekends and public holidays excluded) or receipt of the item or it would be replaced free of charge. If the repair was not covered by the manufacturer's

warranty, SmartStore credits the customer a maximum of $100 towards any service fee charged;

(b) A reduction in the number of advance instalments required before receiving the goods, while the customer remains a "member in good standing"; and

(c) up to $200 annually of technical support on any items purchased.

[33] In adition, Smart Club membership also offered the consumer access to exclusive deals and offers, entry into a monthly prize draw, and a two week payment holiday over the Christmas holiday period (if requested).

[34] The Smart Club membership was an extended warranty agreement, as defined by s 36T FTA. As such, SmartStore was required to provide certain information about the extended warranty agreement, but it failed to do so.

(a) It failed to set out on the front page of the Smart Club membership form:

(i) a summarised comparison between the relevant CGA guarantees and the protections provided by the extended warranty agreement;

(ii) a summary of the consumer's rights and remedies under the CGA;

(b) It failed to set out in the agreement:

(i) the duration and expiry date of the agreement (including whether or not the agreement expires when a claim is made); and

(ii) the total price payable under the agreement.

Detriment to debtors

[35] SmartStore's conduct has caused harm to its debtors. It sells its products to consumers who are often unable to obtain credit from normal retail outlets and are therefore in a position where they pay highly inflated prices to acquire electronic goods. SmartStore's inadequate initial disclosure (and in the instances where the Credit Contracts were varied, the variation disclosure) about the Credit Contracts means that these debtors may not fully understand the cost of purchasing the electronic goods. The debtors will have likely been unaware of the impact of the additional fees and charges on their account balance and, in instances where they have defaulted, the impact of the default fee of $15. SmartStore advised that around 55 percent of debtors were in arrears and therefore incurring such default fees.

[36] Further, the misleading representations about the debtor's rights under the Credit Contracts means that they are unlikely to exercise the rights accorded to them by the CGA, because the express terms of the Credit Contract does not appear to allow them to do so.

[37] The failure to properly disclose information about the Smart Club membership means that the consumer is unable to properly and fairly assess whether that membership is worth the weekly payment of $5, which is a significant additional amount in the context of regular instalments of between $20 and $50 per week.

Gain to SmartStore

[38] SmartStore has provided information to the Commission that it generated total income of $2,881,702 and gross profit of $2,299,154 for the 2015 financial year. It received $436,489 in fees from debtors/consumers between 25 February and 31 October 2015.[1]

[1] It is acknowledged that there is a discrepancy between the number of contracts in respect of which establishment, delivery and administration fees were charged. It is not clear whether this is because of an administrative or accounting error, because certain fees were not charged in a small number of cases, or some other reason.

(a) $170,034 in relation to establishment fees charged in respect of 2415 contracts;

(b) $58,250 in relation to delivery fees charged in respect of 2302 contracts;

(c) $44,295 in relation to administration fees charged in respect of 2356 contracts;

(d) $87,255 in relation to dishonour fees charged in respect of 1473 contracts;

(e) $76,655 in relation to Smart Club membership fees charged in respect of 1209 contracts.

[39] Where a creditor has failed to comply with ss 17 or 22 CCCFA, it cannot enforce any payment due under the contract until such disclosure is provided, and even after then no payment can be enforced for fees such as the administration and dishonour fees (to 5 June 2015), or for the costs of borrowing (from 6 June 2015), for the period during which the creditor has failed to comply. As SmartStore has not complied with ss 17 or 22 CCCFA, debtors have paid, and SmartStore has received, establishment, delivery, administration and dishonour fees totalling $359,804 that it was not entitled to receive.

[40] SmartStore was also not entitled to charge default fees to debtors because of the insufficient disclosure. Pursuant to s 99 CCCFA, SmartStore cannot enforce credit contracts until disclosure is given in compliance with the Act. It therefore received $87,255 in dishonour fees that it was not entitled to receive.

[41] Pursuant to s 36V FTA, where a warrantor has failed to provide the information required by s 36U FTA, a consumer may cancel the extended warranty agreement at any time and the warrantor must immediately repay all additional consideration paid by the consumer. On the basis that each of the 1209 consumers who entered into Smart Club memberships between 25 February and 31 October

2015 was or is able to cancel their memberships, then SmartStore was or is liable to refund up to $76,655 in membership fees.[2] The Commission accepts, however, that SmartStore is not liable to refund the membership fees until a consumer cancels his or her membership.

Defendant's statement

[42] During a voluntary interview with the Commission on 6 October 2015, SmartStore representatives stated that the company:

(a) Charges higher prices for its products to subsidise those who do not meet all their payments;

(b) Had deleted a clause in the "Smart Club membership" document that extended the term of the manufacturer's warranty by 12 months, believing this change meant that the product was no longer an extended warranty;

(c) Disputed that clauses in the Credit Contract Disclosure document were misleading about debtors' rights under the CGA;

(d) Had the Smart Club membership and Credit Contract Disclosure documents reviewed by legal counsel; and

(e) Did not appreciate that payments set out in the Credit Contracts were insufficient to pay off the loans, but would look to fix the issue.

Submissions

[43] The Commerce Commission submits that in determining the penalty to be imposed the context in which this offending has occurred is relevant. That is so, says the Commission, because the defendant was investigated as part of a wider

[2] As noted above, the charges relating to breaches of s 36U of the FTA begin from 1 June 2015. It is unclear how many of the 1209 Smart Club memberships were active during the charge period, and therefore the total amount of membership fees that SmartStore was or is liable to refund.

investigation of the mobile trader industry. The resulting report was widely publicised and referred to widespread non-compliance with the Credit Contracts and CCCFA. Non-compliance was said to be especially prevalent with regard to mandatory disclosure observations. Compliance advice was provided to Mobile Traders and the defendant. This context, submits the Commission, makes the offending serious.

[44] The misrepresentation charges relate to 2415 contracts and are thus the lead charges. The Commission submits that there were affirmative misrepresentations and that the provisions of s 99 illustrates that this is not just technical offending. So the Commission submits that the starting point that the Court ought to adopt for all of the offending should be a fine in the region of $260,000 to $300,000 adjusted for totality down to $200,000 to $240,000. The Commission accepts that an overall discount of somewhere in the region of 30 percent combining a discount for guilty plea and co-operation and presumably by implication, a lack of any previous convictions, ought to be applied by the Court.

[45] Mr Carter has filed helpful submissions and a detailed affidavit from Mr Hence, a director of the defendant. He has made oral submissions in addition to his written submissions. At least in part his submissions suggest that the Court ought to approach if not the first group of charges then certainly the balance as somewhat technical breaches.

[46] Specifically he submits:

(a) That the starting point for sentencing submitted by the Commerce Commission is too high taking into account previous case law and the totality principle;

(b) This is the defendant's first offence;

(c) There are no aggravating factors which require any sort of uplift from the starting point for sentencing;

(d) There are a number of mitigating factors which justify a significant reduction from the starting point adopted. Those mitigating factors relied upon include:

(i) the defendant's early guilty pleas;

(ii) the defendant's cooperation with the Commerce Commission;

(iii) the defendant's attempts to comply and obtain legal advice and its innocent reliance on that advice to its detriment;

(iv) the defendant ceased trading once notified of its breaches by the Commission.

(v) the defendant's substantial efforts to remedy its breaches (including taking full and comprehensive legal advice);

(vi) the defendant's remorse;

(vii) the actual level of harm caused being relatively low; and

(viii) the non-deliberate nature of the offending.

(e) Having regard to all the circumstances and previous case law the Court should impose a sentence that includes a reasonably significant reduction from the starting point adopted for sentencing.

[47] The defendant responds to and disputes the aggravating features said to be identified by the Commerce Commission's submissions. It says instead that at least to some extent the Commission has identified elements of the offending as aggravating factors. One of the key features of the submissions made on behalf of the defendant is that it claims to have been originally proactive in employing a compliance officer, Mr Freeman. Relying largely on that it denies any high degree of negligence but, of course, that has to be measured against compliance advice received from the Commission itself. It is suggested that although a lot of customers

were mislead, taken in isolation each breach did not involve serious negligence and it is submitted that therefore an accumulation of numbers does not lead to a higher degree of negligence. With the greatest of respect, in my view, that offends against common sense. Repeated negligence, even if the contract is not specifically drafted for each customer, must increase culpability in my view. For it to be otherwise might suggest that an offender could enjoy some kind of immunisation for repetitive offending and that cannot be so. Culpability has to be sensibly assessed.

[48] The defendant makes the submission that corrective disclosure has been made. Again, with respect, I do not see that as mitigating. It is, in reality, no more than an action reflecting a requirement of the law. Failing to correct may have been an aggravating factor but of course that is not the case here. But to do so does not itself mitigate. At best it reflects the absence of an aggravating factor that might otherwise have increased the starting point.

[49] There is an affidavit that I have already mentioned, sworn and filed by Mr Hence as director of the defendant company. I do not propose to go through that affidavit in any particular detail but Mr Hence deposes to the company providing a helpful and useful service centre to customers, or rather for customers to contact if they had any issues with their product or their account; that the company engaged with each customer individually in order to agree on the most appropriate terms on which the defendant could sell product to the customer; that it worked with customers who faced legitimate payment/repayment difficulties. Mr Hence went on to say that, "It realises that many of its clients come from financially limited backgrounds and always tries to engage with its clients to work out a suitable solution to any of their reasonable problems." The defendant, through Mr Hence, expresses remorse. The affidavit then goes on to talk about the employment of Mr Freeman, the consultant, who it was thought had expertise in compliance issues. He was first met by Mr Hence in 2012. The company was first contacted by the Commerce Commission in relation to possible breaches of the credit contracts of the CCCFA in April 2013.

[50] Mr Hence deposes to the fact that immediately upon being contacted by the Commerce Commission the defendant forwarded all correspondence to Mr Freeman

and gave him full responsibility to deal with the Commerce Commission. The company's first meeting with the Commerce Commission was on 14 January 2014. Mr Hence repeats that Mr Freeman was given full responsibility by the company or at least its predecessor and later the defendant to effect those changes required by the Commission and communicate with the Commission on behalf of the defendant in order to ensure the documentation was compliant. It is said that Mr Freeman took more of a role as matters became more serious.

[51] Specifically, Mr Hence had this to say:

> 19 On 7 May 2014 the CC wrote to SDLL with the outcome of its review of Smart Store's customer documentation (letter annexed and marked "D"). The CC advised that it was concerned that Smart Store's documentation did not comply with the CCCFA and FTA.
>
> 20 Smart Store agreed with Mr Freeman that he would amend any necessary documentation to ensure compliance.
>
> 21 During this time Mr Freeman continued to correspond on Smart Store's behalf and deal with the CC's requests and complaints from customers. Smart Store relied on Mr Freeman to deal with compliance and ensure the requirements of the CCCFA and FTA were met.

[52] While it has been submitted that the company had good cause for relying on the advice and assistance being received by Mr Freeman the reality is that Mr Hence himself received a letter dated 7 May 2014 from the Commission which in my view made it quite clear that Mr Freeman's drafting abilities were wanting. In two places in that letter it was recommended that the company seek legal advice in order to comply with the law. The flavour that I discern is that Mr Hence, who in reality personifies the defendant, handed over responsibility for compliance to Mr Freeman. That occurred when he, as director, not Mr Freeman as a contractor or employee, remained responsible for the company's activities. There was an abdication of proper control and responsibility at a time when it was plain that the Commerce Commission had raised concerns. It seems to have been done in the way set out in paras 19, 20 and 21 quoted above.

[53] However, it must have been apparent, or at least should have been apparent to Mr Hence and thus the defendant, that Mr Freeman's amended documents were

seriously wanting and did not comply with the law. That is apparent from that letter to which I have just made reference. It is quite apparent that Mr Freeman had been involved in the drafting of documents and it was quite apparent that the results were noncompliant. It seems that Mr Freeman had been hired in some capacity from April 2013. So the upshot of all of that is, in my view, that the defendant knew that Mr Freeman's work was questionable and that the Commerce Commission continued to have concerns. Hiding behind or shifting blame partly to Mr Freeman does neither the defendant nor Mr Hence any credit in the sense of proper mitigation in the particular circumstances here. I do not accept the statement in the affidavit and I quote, "At no point in time did the defendant have any reason to doubt Mr Freeman's skills or advice." [Para 33]. At the very least there was an inappropriate abdication of responsibility to Mr Freeman and lack of proper oversight. What is to the credit of the defendant is that it stopped trading pending its lawyer's review of the documentation. That, of course, was after it had been told that it was being prosecuted. Those steps taken to become a compliant entity and the continuing steps that the company have adopted are mitigating.

[54] The submissions as to the starting point by the defendant include drawing to the Court's attention various cases. In my view in this area comparison is difficult in respect of cases referred to and I will come back to that. However, ultimately the defendant submits that for the s 13 FTA offending I should adopt a starting point of $100,000 to $140,000 fine. For the s 22 and 17 CCCFA offending a starting point in the range $40,000 to $60,000. For the s 36U FTA offending, a starting point in the range of $20,000 to $30,000 resulting, it is submitted, in a global starting point range of $160,000 to $230,000 which it is submitted I should adjust the totality down to a starting point in the range of $100,000 to $150,000 before taking into account mitigating factors.

[55] The defendant then submits that there should be a 25 percent discount for guilty plea, that of course is the last calculation that the Court should make rather than the first. But little, if anything, turns on that. I am asked also to give a discount for co-operation and efforts to reform and I am asked to give a discount to take into account the employment of the so-called compliance officer, Mr Freeman. To do that at this stage would, in my view, be double counting. That is not a mitigating

factor but rather a factor that if I took it into account would assist in setting the original starting point. I am also asked to take into account the fact that the company ceased trading immediately it knew that it was being prosecuted. I am asked to take into account the genuine remorse expressed by the company through Mr Hence's affidavit. I am asked to take into account the relatively low level of harm said to have occurred although in my view that is more appropriately dealt with in assessing the original culpability and starting point rather than as a mitigating factor. The remedial efforts are drawn to my attention. I accept that those occurred and that there has been significant corrective measures, refunds and credits. It is also submitted that there was a lack of deliberation in the offending. Again, with respect, is not so much a mitigating factor as something that has to be taken into account in setting the original starting point. In any event, overall it is submitted that I should adopt a 35 percent discount to take into account these mitigating factors from whatever starting point is adopted.

Discussion

[56] The features in forming the overall culpability here are firstly the context in which this offending took place. There was a widely publicised report and all of this occurred in the context of mandatory disclosure requirements that are not especially difficult. In any event, no such argument, as I understand the position, has been proffered. In other words it has not been suggested that the rules are especially difficult. Any person or company embarking on activity in credit finance, especially where heavily inflated prices are adopted, can expect close scrutiny. That is even more so where there are potentially vulnerable consumers and communities where recourse to mainstream retail is less available. There are two examples in the summary of facts of breathtakingly overpriced common items and no dispute has been raised in relation to that statement in the summary of facts. In my view this virtually automatically raises the spectre of a gullible, vulnerable consumer.

[57] Secondly, and really as part of the context, the FTA is now more or less three decades old. Penalties were increased in 2013 by Parliament trebling the penalty. The message that deterrence is required could not be clearer.

[58] Thirdly, the misrepresentations involved 2415 contracts. Compared with large national or multi-national companies that number is not large but it more or less represents that many individuals having being misled. The CCCFA is, more or less, a decade old. Extended disclosure requirements were enacted in 2014 with a one year lead time before coming into force in June 2015. This legislation is there to address the imbalance between consumer and creditor knowledge and information. It is the case that one explanation for poor decision making by consumers regarding credit is or has been poor protection from inadequate disclosure. The Minister said as much when introducing the 2014 amendment bill. As I touched on earlier, a consumer at the vulnerable end of the consumer credit market willing to pay a vastly inflated purchase price on credit must be treated with scrupulous care and accuracy. I am satisfied that was the case here, at least on occasions. The power, sophistication and commercial nous was with the defendant not the purchasers. Advantage was taken of that imbalance 2415 times, more or less.

[59] Around 55 percent of customers were in default and incurring default fees. Substantial commercial gain has accrued. Although the figure may not necessarily be entirely accurate, the differences are not material, but it seems that $436,489 was accrued to the defendant. This is telling when deterrence is so important in this area of asymmetrical commerce. The misrepresentations were significant and there were four of them in each contract. It is not an adequate answer to hide behind advice supposedly taken and that is especially so when the breaches are clear and illuminated by the Commerce Commission investigation and advice given and wide publicity disseminated.

[60] The schedule 1 disclosure charges related to failure to disclose six key pieces of information. The variation disclosure charges related to three specific contracts and again relate to failure to disclose or disclose adequately six pieces of information. The extended warranty charges relate to 700 to 800 agreements over about a five month period. These breaches and this offending in total significantly undermine the protections afforded to consumers and were widespread. The defendant's actions in relation to the misrepresentation charges amounted, in my view, to gross negligence and came perilously close to recklessness. I am

unconvinced that using Mr Freeman in all the circumstances of this case mitigates. There was a similar degree of fault in the balance of the offending.

[61] In assessing individual starting points and a resulting global starting point I have borne in mind the need to determine the seriousness of the offending and make a comparison to other cases where such an approach is realistic. I have considered all the cases that have been referred to me and I have taken particular note of para [9] of the judgment in *Commerce Commission v Tiny Terms Ltd* DC Auckland CRI-2012-004-011709, 24 January 2014 which reads thus:

> However, there are limits to which the previous cases can go in providing assistance to this sentencing. Those limits include, firstly there is not yet, as far as I am aware, a decision of the High Court in terms of s 17 and s 32 CCCF Act. Secondly, some of the cases predate the sentencing methodology mandated by the Court of Appeal in *R v Taueki* [2005] 3 NZLR 372 (CA) and *R v Clifford*. Third, some of the cases involved agreed starting points. Fourthly, they involve various combinations of the Acts, sections and numbers of charges. Fifth, there is generally a pattern of deciding on global culpability and then apportioning that per information. Sixth, one case only appears to have been decided post the Supreme Court decision in *Hessell v R* [2010] NZSC 135, [2011] 1 NZLR 607. Finally, as Mr Hamlin points out, the Commission has often got the difficult task of deciding just how to structure the charges, the number of charges, the extent to which they are representative in fairly but firmly prosecuting these matters.

[62] In a decision released, I believe in the last day or so, Judge Collins further explained that paragraph in a decision *Commerce Commission v Ace Marketing Limited* CRI-2016-004-002128 [2016] NZDC. In explaining or expanding upon para [9] from *Tiny Terms* he had this to say at para [59]:

> I record in this judgment a comment about the decision in *Tiny Terms*. The defendant in that case was closely associated with Love Springs Ltd. That is noted in the judgment. It was Love Springs that actually sold the water cooler units and effectively assigned the financing or lease to buy rights to Tiny Terms. Love Springs Limited and Tiny Terms Limited had the same effective beneficial ownership. Love Springs and its managing director had separately faced charges under the FTA for making very serious and false allegations about tap water. They did that so as to promote the sale of the water coolers. On a combined basis fines of approximately $500,000 were imposed on Love Springs and its managing director. My error in delivering the *Tiny Terms* judgment was not to make it clear that the Tiny Terms offending had to be viewed in the light of what had already gone before and had been imposed on the associated entities. Had Tiny Terms stood on its own I would have unquestionably imposed higher penalties. *Tiny Terms* does not provide the level of assistance here that counsel suggest but the fault for that lies with me. What I have had to say in this judgment about

> Tiny Terms only reinforces the view that I have that because the cases vary so much on their facts that earlier cases, unless they be those of the Higher Courts, have their limitations in the setting of the appropriate starting point.

[63] Once I have fixed a starting point, of course, I will then need to identify the mitigating factors and if necessary consider the defendant's ability to pay. I do not understand that the latter has been raised as an issue in this case. There has been relevantly a three-fold increase in penalties for the corporate entities, from $200,000 to $600,000 under the FTA enacted in 2013 and which came into force on 16 June 2014.

[64] I had this to say in the case of *Commerce Commission v Budge Collection Limited and Sun Dong Kim* at para [38].

> It is self-evident that the Court must reflect Parliament's intention and the approximate three-fold increase in penalties although to do so does not require a simple multiplication of what might otherwise have been the starting point under the previous regime. Nevertheless on any analysis a substantial increase to sentencing levels is called for to reflect Parliament's clear intention.

[65] Finally, before setting the starting point and concluding I note the well understood purposes of the legislation encapsulated in *R v Senate Finance Ltd* DC Auckland CRN 2006-450-2955, 14 November 2006 where the Court observed the purposes of both acts of Parliament are 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 misrepresentations and unfair practices. Consumers must be adequately informed of their rights and responsibilities. Consumer rights to disclosure of information developed over the last few decades prescribe that anything that is material in a contractual relationship between a vendor and purchaser or a shop keeper and a customer must be made clear and conspicuous in the interests of fairness and honest trading.

Now those concepts underpin both pieces of legislation.

[66] The starting points, in my view, submitted as appropriate by the Commerce Commission are couched in terms of a range and are realistic and appropriate. For the charges under s 13(i) and s 40(1) FTA, where the maximum penalty is $600,000, I consider that an appropriate global starting point is $150,000. For the CCCFA

offending there were many contracts and multiple breaches in each. The starting point should be $70,000. The starting point for the s 36U FTA which also carries the maximum penalty of $30,000, again there were many affected debtors over a five month period where there was absolutely no disclosure, the starting point should be $40,000. Those starting points are $260,000 in total. There needs to be a significant adjustment to reflect the totality of the offending. The resulting starting point should therefore be, overall, a fine of $200,000. I allow a 10 percent discount for co-operation, remediation, remorse and lack of prior convictions. From the notional result of $180,000 I give a discount of 25 percent for guilty pleas. That reduces the fine by $45,000 down to $135,000 which I apportion as follows; for the false and misleading representations, that is CRNs 2884, 2885 and 2886, on each of those the defendant is fined $36,000 and ordered to pay Court costs of $130 on each. For the s 17 breaches of the CCCFA disclosure requirements, that is CRNs 2878, 2879 and 2880, the defendant is fined $4000 and on each also ordered to pay $130 Court costs. For the s 22 breaches of the CCCFA disclosure requirements, that is CR numbers ending 2881, 2882 and 2883, the company is fined $4000 and on each ordered to pay $130 Court costs. On the remaining two charges being breaches of s 36U(1) of the FTA disclosure requirements, that is CR numbers ending 2887 and 2888, the company is fined $1500 on each and ordered to pay $130 Court costs.

R G Ronayne
District Court Judge