

9 December 2015

Walter Gollan Limited, trading as Gollan & Co Finance
71-73 Onehunga Mall
Auckland 1061

Attention: Andrew Reid, Director

Dear Mr Reid

Credit Contracts and Consumer Finance Act 2003 and the Fair Trading Act 1986: Warning and compliance advice

The Commerce Commission has been investigating the conduct of Gollan & Co Finance (Gollans) under the Credit Contracts and Consumer Finance Act 2003 (CCCFA) and the Fair Trading Act 1986 (FTA). The investigation has now been completed and we write to alert you to our concerns.

Summary

The Commission considers that Gollans is likely to have breached:

- section 17 of the CCCFA by failing to provide borrowers with initial disclosure of applicable information about their consumer credit contracts;
- section 22 of the CCCFA by failing to provide borrowers with disclosure about changes to their loan contracts when additional borrowings were added to the original loan balance; and
- section 13(i) of the FTA by providing false or misleading information to borrowers.

The Commission also has concerns that Gollans is at risk of having breached:

- section 41 of the CCCFA relating to unreasonable fees; and
- section 51 of the CCCFA relating to full prepayments.

After carefully weighing up the factors set out in our Enforcement Response Guidelines, we have decided to conclude this investigation by issuing this warning letter and providing

AUCKLAND

L19, 135 Albert Street
P.O. Box 105-222
AUCKLAND 1143
NEW ZEALAND
2174296.1

WELLINGTON

L6, 44 The Terrace
P.O. Box 2351
WELLINGTON 6140, NEW ZEALAND
Tel: (04) 924 3600 Fax: (04) 924 3700
Main Office

CHRISTCHURCH

L1, Unit 17 Barry Hogan Place
55 Princess Street, Riccarton
P.O. Box 9237, Tower Junction
CHRISTCHURCH 8149, NEW ZEALAND

advice to assist Gollans to meet its statutory obligations. We will not be taking any further enforcement action against Gollans at this time.

We acknowledge that Gollans has taken steps to refund customers some of the establishment fees charged, and we have taken that into account in reaching our decision.

The investigation

Our investigation has established that Gollans operates from Onehunga, Auckland and provides consumer and small business loans to a limited number of customers. It does not advertise and its borrowers are repeat customers or referrals from existing customers. Gollans advances approximately 10 consumer loans each year for an average term of two years. In the period 2005 to 2015 it advanced approximately 70 consumer loans. Loan finance is sourced from family money.

Gollans documents its loans on a form entitled "Gollan & Co Finance Deed by Way of Security" which contains references to the Credit Contracts Act 1981, the Hire Purchase Act 1971 and a "finance rate".

As part of the investigation, we considered information provided by Gollans and reviewed sample copies of contracts for its consumer loans.

The contracts predate changes to the CCCFA, which came into effect on 6 June 2015. Accordingly, the changes do not apply to the loan contracts that the Commission has reviewed.

The Commission's view

Gollans' contracts for its consumer loans meet the definition of a consumer credit contract set out in section 11 of the CCCFA. As noted above, the Commission considers that Gollans is likely to be in breach of the CCCFA and the FTA in a number of respects.

Relevant sections of the CCCFA and the FTA, referred to in this letter, are set out in Attachment 1.

Likely breaches of the CCCFA and the FTA

CCCFA Section 17 - Initial disclosure

Section 17 of the CCCFA requires lenders to provide borrowers with disclosure of key information applicable to the loan. A list of potentially applicable key information is set out in Schedule 1 to the CCCFA.

The contracts we have reviewed do not meet the disclosure requirements of section 17. Specifically, they do not contain the following applicable key information:

- an explanation about how the loan interest is calculated and frequency with which interest charges will be debited (clause (k) Schedule 1);

- an explanation of how the reasonable estimate of the lender's loss on full prepayment is calculated and whether the statutory procedure set out in the CCCF Regulations is used (clause (p) Schedule 1); and
- a statement of the borrowers' right to cancel the loans under section 27, in the format prescribed by clause (s) of Schedule 1.

Some individual loan contracts are also missing the date on which the first payment is due, the frequency of subsequent payments (clause (o) of Schedule 1) and one loan showed an incorrect figure for the amount borrowed.

CCCFA Section 22 – variation disclosure

Section 22 of the CCCFA requires lenders to disclose agreed loan changes to borrowers. Our investigation has found that Gollans does not always provide such disclosure.

Loan account statements reviewed during the investigation show that two of Gollans' borrowers have had a total of 19 additional advances for sums ranging from \$150- \$3000. These amounts appear to have simply been added to existing loans, presumably on the same terms and conditions as the original advance, but there is no evidence that the borrowers were provided with updated documentation as required by section 22.

FTA Section 13(i) – false or misleading representations

Section 13(i) of the FTA prohibits parties in trade from making false or misleading representations about the existence of any right or remedy in connection with the supply of goods and services.

Gollans' loan contracts refer to borrowers having rights under both the Credit Contracts Act 1981 and the Hire Purchase Act 1971. Both Acts were repealed by the CCCFA in 2005 so the reference to borrowers having rights under those Acts is likely to constitute a false representation in breach of section 13(i).

Warning

This letter constitutes a formal warning. The Commission considers that Gollans' conduct with regard to the issues discussed above is likely to breach the CCCFA and/or the FTA.

In the circumstances of this case, we have decided to conclude our investigation by issuing you with this warning. We will not be taking any additional action.

We would, however, take this warning into account if such conduct were to continue or if you were to engage in similar conduct in the future. We may also draw this warning to the attention of a court in any subsequent proceedings brought by the Commission against Gollans.

Compliance advice regarding potential breaches of the CCCFA

In addition to the issues discussed above, the investigation has also disclosed issues which may put Gollans at risk of breaching the CCCFA in other respects. The following section of this letter outlines our concerns in this regard and provides advice to assist Gollans to comply with its statutory obligations in the future.

In summary, we consider that Gollans' calculation of its DOC and DRL fees and its prepayment amounts may breach:

- section 41 of the CCCFA which prohibits charging unreasonable credit fees; and
- section 51 of the CCCFA which relates to full prepayment amounts.

Section 41 – credit fees cannot be unreasonable

Section 41 of the CCCFA prohibits credit fees which are unreasonable.

Gollans usually charges borrowers two fees upon the establishment of a loan – an Establishment/Documentation fee (DOC fee) and a Debt Recovery Levy (DRL).

The DOC and DRL fees vary from loan to loan. The loans reviewed show DRL fees ranging from \$0-\$1500 and DOC fees ranging from \$200-\$800. In total, Gollans has received approximately \$32,500 in establishment fees since the CCCFA took full effect on 1 April 2005.

The test for reasonableness of an establishment fee is set out in section 42 of the CCCFA.

In general terms, establishment fees should reflect a lender's reasonable costs in connection with the application for credit, processing and considering that application, documenting the consumer credit and advancing the credit.

In the Commission's view, establishment fees which cannot be linked to the direct costs of providing credit may place a lender at risk of breaching section 41.

Gollans has acknowledged that its establishment fees have not been based on the costs it incurs in providing credit to consumers. Rather, they have been based on a range of factors, including the amount borrowed and the perceived risk of the borrower.

The Commission notes that Gollans has refunded DRL fees totalling \$13,487.61 to 23 borrowers since becoming aware of potential problems with its establishment fee calculations.

Section 51 – amount required for full prepayment

The Commission also has concerns about the way in which Gollans calculates the amount payable upon prepayment of a loan.

Under section 50 of the CCCFA, a borrower has the right to prepay a loan at any time. The methodology for calculating the amount payable is set out in sections 51-54 of the CCCFA. Section 51(2) states that loan interest can only be charged up until the date of prepayment.

Gollans does not calculate loan prepayment amounts in accordance with the CCCFA methodology. Rather, it calculates a rebate of interest using the Rule of 78.

The Rule of 78 provides only an approximation of the loan interest owing and does not accurately calculate the interest due on any particular date. In practice, Gollans also rebated fees, and this appears to have ameliorated any detriment to borrowers. However, the Commission considers that calculating loan prepayment amounts using the Rule of 78 is no longer acceptable and puts Gollans at risk of breaching section 51(2) of the CCCFA.

The Commission's role

The Commission is responsible for enforcing and promoting compliance with a number of laws that promote competition in New Zealand, including the CCCFA and the FTA. The CCCFA regulates the provision of consumer credit and the FTA prohibits false and misleading behaviour by businesses in the promotion and sale of goods and services.

Penalties for breaching the CCCFA and the FTA

Only a Court can decide if there has actually been a breach of the CCCFA or the FTA and a Court can impose penalties where it finds the law has been broken.

Lenders who breach the CCCFA may:

- be unable to enforce the contract or any right to recover property or any security interest
- have to refund money or pay compensation
- have to pay statutory damages
- be convicted of a criminal offence and fined up to \$600,000 per offence for companies and \$200,000 for individuals.
- have contracts changed by the court if the contracts are oppressive
- be banned from operating within the finance industry.

Parties who breach the FTA can be fined up to \$600,000 per offence in the case of a company and \$200,000 for individuals.

You should be aware that the decisions outlined in this letter do not prevent any other person or entity from taking private action through the courts.

This letter is public information and will be published on our website. We may also make public comment about our investigations and conclusions, including issuing a media release or making comment to media.

We note that Gollans is no longer providing loans to consumers. Should you decide to resume consumer lending, we recommend that you seek legal advice.

Further information

We have published a series of fact sheets and other resources to help businesses comply with the CCCFA and the other legislation we enforce. These are available on our website at www.comcom.govt.nz. We encourage you to visit our website to better understand your obligations and the Commission's role in enforcing the CCCFA and FTA.

You can also view the CCCFA and other legislation at www.legislation.co.nz.

Thank you for your assistance with this investigation. Please contact Nicola Schaab on 09 920 3491 or by email at nicola.schaab@comcom.govt.nz if you have any questions about this letter.

Yours sincerely



John Lyall
Manager
Competition Branch
Auckland

Credit Contracts and Consumer Finance Act 2003

11 Meaning of consumer credit contract

- (1) A credit contract is a consumer credit contract if—
- (a) the debtor is a natural person; and
 - (b) the debtor enters into the contract primarily for personal, domestic, or household purposes; and
 - (c) 1 or more of the following applies:
 - (i) interest charges are or may be payable under the contract:
 - (ii) credit fees are or may be payable under the contract:
 - (iii) a security interest is or may be taken under the contract; and
 - (d) when the contract is entered into, 1 or more of the following applies:
 - (i) the creditor, or one of the creditors, carries on a business of providing credit (whether or not the business is the creditor's only business or the creditor's principal business):
 - (ii) the creditor, or one of the creditors, makes a practice of providing credit in the course of a business carried on by the creditor:
 - (iii) the creditor, or one of the creditors, makes a practice of entering into credit contracts in the creditor's own name as creditor on behalf of, or as trustee or nominee for, any other person:
 - (iv) the contract results from an introduction of one party to another party by a paid adviser or broker....

17 Initial disclosure

- (1) Every creditor under a consumer credit contract must ensure that disclosure of as much of the key information set out in Schedule 1 as is applicable to the contract is made to every debtor under the contract—
- (a) before the contract is made; or
 - (b) within 5 working days of the day on which the contract is made.

- (2) Every creditor under a consumer credit contract must ensure that a copy of all of the terms of the contract not disclosed under subsection (1) (other than terms implied by law) is given or sent to every debtor under the contract—
- (a) before the contract is made; or
 - (b) within 5 working days of the day on which the contract is made.....

22 Disclosure of agreed changes

- (1) Every creditor under a consumer credit contract must ensure that disclosure of the following information is made to every debtor under the contract if the parties to the contract agree to change the contract:
- (a) full particulars of the change:
 - (b) any other information prescribed by regulations to be information that must be disclosed under this section.
- (2) Disclosure under this section must be made before the change takes effect.
- (3) Disclosure is not required under this section in relation to a change that—
- (a) reduces the obligations that the debtor would otherwise have, unless the obligations are reduced following an application under section 55; or
 - (b) extends the time for payment of any payment to be made under the contract, unless the time for payment is extended following an application under section 55; or
 - (c) releases the whole or any part of a security interest relating to the contract; or
 - (d) changes the place where payments are to be made.

41 Unreasonable credit fee or default fee

- (1) A consumer credit contract must not provide for a credit fee or a default fee that is unreasonable.
- (2) If the Court is satisfied, on the application of the Commission, a debtor, or a guarantor, that a credit fee or default fee is unreasonable it may order that the fee be annulled or reduced...

42 Establishment fees

In determining whether an establishment fee is unreasonable, the Court must have regard to—

- (a) whether the amount of the fee is equal to or less than the creditor's reasonable costs in connection with the application for credit, processing and considering that application, documenting the consumer credit contract, and advancing the credit; or
- (b) whether the amount of the fee is equal to or less than the creditor's average reasonable costs of the matters referred to in paragraph (a) for the appropriate class of consumer credit contract.

50 Debtor's right to full prepayment

- (1) A creditor must accept any full prepayment of a consumer credit contract from a debtor at any time.
- (2) The full prepayment must be credited in accordance with section 46(1).
- (3) A consumer credit contract must not prohibit the full prepayment of the contract.
- (4) Nothing in sections 97 to 99 of the Property Law Act 2007 limits this section or section 51.

51 Amount required for full prepayment

- (1) The amount required for the full prepayment of the consumer credit contract must be no more than the sum of the following less the amount referred to in section 52:
 - (a) the unpaid balance at the time of the full prepayment; and
 - (b) if expressly authorised by the contract, the administrative costs incurred by the creditor arising from the full prepayment or a charge equal to the creditor's average administrative costs arising from full prepayments of consumer credit contracts of the appropriate class; and
 - (c) if expressly authorised by the contract, a fee or charge that does not exceed a reasonable estimate of the creditor's loss arising from the full prepayment.

- (2) In calculating the unpaid balance, the creditor must only include interest charges and other fees and charges that have accrued or would ordinarily be payable under the consumer credit contract up to the time of the full prepayment.

52 Rebate of insurance

- (1) The amount to be deducted under section 51 is an amount equal to a proportionate rebate of the premium paid under any consumer credit insurance contract financed under the consumer credit contract.
- (2) The rebate must be calculated using the procedure prescribed for the purposes of this section by regulations if regulations have prescribed a procedure.
- (3) An amount is to be deducted under subsection (1) only if the creditor has arranged the insurance.
- (4) If an amount is deducted under subsection (1), the creditor may recover the amount from the insurer as a debt due.
- (5) In this section, insurance is arranged by the creditor if 1 or more of the following applies:
 - (a) the creditor or a related company of the creditor is the insurer:
 - (b) the creditor or a related company of the creditor acts as the agent of the insurer in relation to the insurance:
 - (c) the creditor or a related company of the creditor receives a commission in relation to the insurance:
 - (d) the creditor requires the debtor to obtain the insurance from a particular insurer.

53 Termination of consumer credit insurance contract

A consumer credit insurance contract financed under a consumer credit contract is terminated on the full prepayment of the consumer credit contract unless the consumer credit insurance contract—

- (a) provides insurance cover in connection with 1 or more other credit contracts; or
- (b) otherwise provides a benefit to, or insurance cover for, the debtor.

54 Creditor's loss arising from full prepayment

- (1) A creditor must calculate a reasonable estimate of its loss arising from a full prepayment using—
 - (a) a procedure prescribed for the purposes of this section by regulations; or
 - (b) an appropriate procedure set out in the consumer credit contract for calculating that loss.

- (2) If a creditor uses a procedure prescribed for the purposes of this section by regulations, the amount calculated is to be treated in any court and in any proceedings under this Act as a reasonable estimate of the creditor's loss.

Schedule 1**Key information concerning consumer credit contract**s 17

The following information is the key information concerning a consumer credit contract as is applicable:

Full name and address of creditor

- (a) the full name and full address of the creditor:

Initial unpaid balance

- (b) the unpaid balance as at the date that is specified in the disclosure statement as the effective date of the statement, accounting for every payment made by the debtor on or before that date:

- (c) the amount and a description of each advance, charge, or payment accounted for in the unpaid balance disclosed under paragraph (b):

Subsequent advance

- (d) the amount, a description, and timing of each advance to be made after the effective date of the disclosure statement, if ascertainable:

Total advances

- (e) the total of all advances made or to be made in connection with the contract, if ascertainable:

Credit limit

- (f) the credit limit:

Annual interest rate

- (g) the annual interest rate or rates under the contract (with the rate or rates being expressed in terms of a percentage):

- (h) if there is more than 1 rate, how each rate applies:

- (i) if an annual interest rate is fixed for the term or any part of the term of the contract, the period during which the annual interest rate is fixed:

- (j) if an annual interest rate is determined by referring to a base rate, particulars that describe how the annual interest rate is determined, including—

- (i) the name of the base rate or a description of it; and
- (ii) the margin or margins (if any) above or below the base rate to be applied to determine the annual interest rate; and
- (iii) where and when the base rate is published or, if it is not published, how the debtor may ascertain the rate; and
- (iv) the current annual interest rate or rates:

Method of charging interest

- (k) the method of calculating interest charges payable under the contract and the frequency with which interest charges are debited under the contract:

Total interest charges

- (l) the contract would, on the assumptions prescribed by regulations, be paid out within 7 years of the date on which credit is first provided under the contract):

Interest free period

- (m) if the contract involves an interest free period, the following particulars:
- (i) the length of the interest free period:
 - (ii) when interest will begin to accrue:

Credit fees and charges

- (n) a description of the credit fees and charges (other than interest charges) that are, or may become, payable under the contract (unless the fee or charge is disclosed under paragraph (c)), including—
- (i) when each fee or charge is payable, if ascertainable; and
 - (ii) the amount of each fee or charge if ascertainable, but, if not, the method of calculation of the fee or charge:

Payments required

- (o) if more than 1 payment is to be made—
- (i) the amount of the payments or the method of calculating the amount; and
 - (ii) if ascertainable, the number of the payments; and
 - (iii) if ascertainable, the total amount of the payments (but only if the contract would, on the assumptions prescribed by regulations, be paid out within 7 years of the date on which credit is first provided under the contract); and
 - (iv) when the first payment is due, if ascertainable, and the frequency of payments:

Full prepayment

- (p) how the reasonable estimate of the creditor's loss on full prepayment is calculated and whether a statutory procedure prescribed in regulations is used:

Security interest

- (q) a description of any security interest that is or may be taken in connection with the contract (including a description of any property that is subject to, or proposed to be subject to, any security interest) and the extent to which the debtor's obligations to the creditor are secured:

Default interest charges and default fees

- (r) particulars that describe any default interest charges and default fees that may be payable under the contract including how and when default interest charges and default fees would become payable:

Debtor's right to cancel

- (s) a statement of the debtor's rights under section 27 in the following form (unless the contract is a revolving credit contract):

“Statement of right to cancel

The Credit Contracts and Consumer Finance Act 2003 gives you a right for a short time after the terms of this contract have been disclosed to you to cancel the contract.

How to cancel

If you want to cancel this contract you must give written notice to the creditor.

*You must also—

- (a) return to the creditor any advance and any other property received by you under the contract (but you cannot do this if you have taken possession of any goods or if you bought any property at an auction or if the contract is for the sale of services that have been performed), or
- (b) pay the cash price of the property or services within 15 working days of the day you give notice.

*Delete if the credit contract does not involve a credit sale.

†You must also return to the creditor any advance and any other property received by you under the contract.

‡Delete if the credit contract involves a credit sale.

Time limits for cancellation

If the disclosure documents are handed to you directly you must give notice that you intend to cancel within 3 working days after you receive the documents.

If the disclosure documents are sent to you by electronic means (for example, e-mail) you must give notice that you intend to cancel within 5 working days after the electronic communication is sent.

If the documents are mailed to you, you must give the notice within 7 working days after they were posted.

Saturdays, Sundays, and national public holidays are not counted as working days.

What you may have to pay if you cancel

If you cancel the contract the creditor can charge you---

- (a) the amount of any reasonable expenses the creditor had to pay in connection with the contract and its cancellation (including legal fees and fees for credit reports, etc); and
- *(b) interest for the period from the day you received the property or services until the day you either pay the cash price for the property or services or return the property to the creditor.

*Delete if the credit contract does not involve a credit sale.

- †(b) interest for the period from the day you received the advance until the day you repay the advance.

‡Delete if the credit contract involves a credit sale.

This statement only contains a summary of your rights and obligations in connection with the right to cancel. If there is anything about your rights or obligations under the Credit Contracts and Consumer Finance Act 2003 that you do not understand, if there is a dispute about your rights, or if you think that the creditor is being unreasonable in any way, you should seek legal advice immediately.”

The Fair Trading Act 1986

13 False [or misleading] representations—

No person shall, in trade, in connection with the supply or possible supply of goods or services or with the promotion by any means of the supply or use of goods or services,—....

- (i) make a false or misleading representation 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 Consumers Guarantees Act 1993...