IN THE HIGH COURT OF NEW ZEALAND
AUCKLAND REGISTRY

CRI-2008-404-210

COMMERCE COMMISSION
Appellant

v

AVANTI FINANCE
Respondent

Hearing: 6 April 2009

Appearances: M Woolford and AM McClintock for Appellant
J Miles QC and I Denton for Respondent

Judgment: 28 April 2009

JUDGMENT OF ASHER J

This judgment was delivered by me on 28 April 2009 at 4:30 pm pursuant to Rule 11.5 of the High Court Rules

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Registrar/Deputy Registrar

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Date

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Introduction

[1] The Commerce Commission appeals by way of case stated a judgment of the District Court of 10 June 2008 dismissing various charges against the respondent, Avanti Finance Limited ("Avanti"). The central question before the District Court was whether for the purposes of ss 51 and 54 of the Credit Contracts and Consumer Finance Act 2003 ("CCCF Act"), Avanti in fixing the amount to be paid if there was an early full prepayment of a loan, breached the requirements of the Act by fixing a formula that did not involve a reasonable estimate of loss. The particular question set out at the end of the case stated is:

> Was the defendant required for the purposes of ss 51 and 54 of the CCCF Act to calculate a reasonable estimate of its loss on the assumption that it will immediately lend the funds prepaid at the then prevailing interest rates even when it has excess lending capacity?

[2] As a case stated, this is an appeal relating to a question of law. The background facts were not much in dispute in the District Court, and the case stated sets out what was proven at the hearing in full. It is not necessary to repeat all the background material or quote the full contents of the case. However, a brief summary of the now uncontested background facts as set out in the case stated is necessary.

The facts of the case stated

[3] Avanti is a relatively small financier operating in the non-bank lending market. It offers a wide variety of loans usually ranging from $1,000 to $30,000. It has a range of customers varying from homeowners with relatively low risk profiles to persons with a poor credit history. The interest rate it charges will turn on a large number of factors which centre on risk. Avanti's interest rates up to the time of the District Court hearing had ranged from 13 to 25 per cent, depending on the perceived risk of the loan.

[4] Avanti obtains funds from four sources. These are retained earnings, its shareholders, debentures and a bank facility. Funds from retained earnings and

shareholders do not appear to figure as a source of funds on a daily basis. Monies available from debenture holders are available for lending and at the time of hearing totalled around $22 million. Importantly, given the issue in this hearing, Avanti had a bank facility with the ANZ National Bank of New Zealand, which was increased on 1 May 2006 from $34 million to $40 million ("the bank facility"). Avanti treats this facility as what is described as a "marginal source of funds". Over the period at issue in relation to the charges against Avanti, the unused portion of the facility ranged between $13.32 million and $20.35 million. Interest on that bank facility was at the 90 day bank bill buy rate plus a margin of 1.9 per cent per annum, and therefore ranged between 8.98 per cent and 9.67 per cent over the period at issue.

[5] When Avanti requires funds beyond its own capital, debenture funds and loan repayments, it draws the funds it requires from the bank facility, which is at all times well in credit. An aspect of this arrangement is the involvement of an company associated with Avanti, Galatos Finance Limited, which has the same shareholders as Avanti, but for the purposes of this case stated appeal it is not necessary to go into the details of that company's involvement.

[6] The prosecution related to 50 credit contracts of Avanti, which were each terminated by the debtor before the contract end date, by the debtors choosing to make a full prepayment of the loan. The contracts were prepaid during an 18 month period from June 2005 to December 2006. The 50 credit contracts were all fixed term and fixed interest rate contracts varying in amounts from $2,093.41 to $43,764.09, and with interests rate varying from 16 to 25 per cent.

[7] Each of the 50 credit contracts contained a clause under the heading "Full Prepayment". It is necessary to set out the terms of the full prepayment clause:

> FULL PREPAYMENT
>
> If you pay the unpaid balance in full before the final payment is due (full prepayment), you may be required to pay a fee or charge to compensate the creditor for any loss resulting from the full prepayment. The creditor may have suffered a loss if the creditor's current interest rate is lower than the interest rate applying to your original consumer credit contract. You may also have to pay the creditor's administrative costs relating to the full prepayment.

The amount you may have to pay to compensate the creditor for the loss is calculated using the following formula:

$$CP = \frac{UB}{1} \times \frac{AR - (NB + 1.9)}{100} \times \frac{90}{365}$$

where	CP	=	Compensation payable
	UB	=	Unpaid balance
	AR	=	Annual interest rate shown in the interest section of this disclosure statement
	NB	=	ANZ National Bank 90 day bill rate previously set on the most recent of the following dates 01 January, 01 April, 01 July and 01 October. If no such rate is available then the 90 day rate so set by any other major registered bank.

NOTE - Should the period remaining on the contract be less than 90 days then the maximum compensation will be adjusted proportionally.

[8] This formula was drafted by Avanti in anticipation of the CCCF Act coming into force. The defendant analysed the prepayments it had experienced prior to that time and found that where there was prepayment, it typically occurred 16.7 months into a 32.4 month term (that is 15.7 months early).

[9] The formula that is set out in the contract was devised with legal advice aimed at ensuring the contract complied with the CCCF Act, and that the prepayment formula was appropriate. Avanti was told that when a loan was prepaid, its loss was all the unearned interest on the loan. So, Avanti developed a formula which would be conservative and which would produce a fee less than that loss. It decided to cap the fee it charged to 90 days interest at the contract rate, less the bank facility interest rate that was available to it at the time. Its goal, therefore, was to recover by an application of the formula, a set part of the profit lost as a consequence of the prepayment.

[10] The underlying assumption of this formula was that whenever a loan contract was prepaid, Avanti would lose the profit that it would have realised during the remainder of the term of the loan. This was because even if the monies were immediately relent, Avanti had excess funds available to meet its operational expenses, interest payments and new loans. There was always a substantial unused

capacity in the bank facility, and this meant that there was always a net loss of a customer in the event of a prepayment.

[11] Avanti had the significant unused bank facility for two reasons. First, it had hoped to increase its business and needed that capacity. Further, having the facility available was prudent management. It meant that Avanti did not have to rely on uncertain short-term cashflows and debenture flows, and always had sufficient capacity to make loans which met its criteria.

[12] The formula had no regard to changes in the creditor's lending rates and did not allow for mitigation of lost profit through relending on a new loan. It did not allow for the fact that the outstanding balance would be reducing over the 90 day period. It made no allowance for the time value of money. Nevertheless, the formula which Avanti developed against this background was conservative and produced a fee that was generally less than its estimate of loss.

The relevant sections

[13] Section 43(2) of the CCCF Act provides:

> **43 Prepayment fees**
>
> …
>
> (2) A fee or charge payable on a full prepayment of a consumer credit contract (other than a fee relating to administrative costs) is unreasonable if, and *only if, it exceeds a reasonable estimate of the creditor's loss arising from the full prepayment* as calculated in accordance with section 54.
>
> [emphasis added]

[14] Section 51 is also relevant. It provides:

> **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.

[emphasis added]

Section 52 relates to rebates of insurance.

[15] Section 54 provides:

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.*

[emphasis added]

[16] Section 43(2), s 51 and s 54 therefore provide that a prepayment fee or charge is unreasonable only if it exceeds a reasonable estimate of the creditor’s loss arising from the full prepayment as calculated in accordance with s 54. Under s 54 the creditor has two options. First, it may use the procedure prescribed for the purposes of the section by regulation. The formula set out in the regulations is known in the industry as the “safe harbour” formula. Alternatively, it can use an “appropriate procedure” set out in the consumer credit contract which must be a reasonable estimate of its loss. This option is not known by any such comforting

name, reflecting the fact that a creditor has to exercise its own judgment as to what is a reasonable estimate of its loss, and to take the risk that if the contractual term it devises is not a reasonable estimate of loss, it may face prosecution and conviction. Given the usual parlance of "safe harbour" for the calculation procedure referred to in s 54(1)(a), I will refer to the formula prescribed in the rules enacted under that section throughout this judgment as the "safe harbour formula".

[17] There has been no New Zealand authority referred to that casts light on the interpretation of s 54.

The issue

[18] Avanti has not chosen the safe harbour, and its formula is exposed to the storms of judicial consideration. The core issue in this case stated is whether Avanti calculated reasonable estimates of loss arising from full prepayment by an appropriate procedure for calculating that loss, namely the prepayment clause. The case stated set out the question as follows:

> 6. The question for the opinion of the Court is whether my decision in so far as it relates to the CCCF Act charges was erroneous in point of law as follows. Both parties accept that a reasonable estimate of loss for the purposes of sections 51 and 54 of the CCCF Act will take account of the common law principles in relation to loss on breach of a contract and a duty to mitigate that loss. Given that, was the defendant required for the purposes of sections 51 and 54 of the CCCF Act to calculate a reasonable estimate of its loss on the assumption that it will immediately lend the funds prepaid at the then prevailing interest rates even when it has excess lending capacity?

It is the last sentence, already quoted, which sets out the real question, but to understand it it is necessary to reiterate an aspect of the background.

[19] Avanti in its prepayment clause assumed that the prepaid funds would not immediately be lent out again at the then prevailing interest rates. Because of the excess capacity provided by the bank facility, its supply of finance exceeded market demand. Thus any new contracts were contracts that would have been secured by Avanti in any event. The effect of an early prepayment therefore meant the loss of

the profit on that contract, as the profit on any new contract that followed would have been enjoyed in any event.

The Judge's reasoning on the issue

[20] The Judge set out her reasoning in the case stated. She concluded that every prudent finance company would clearly have some excess capacity in its sources of funds so that it could survive defaults or prepayments. She accepted as a matter of fact that prepayments by existing debtors during the period covered by the 50 charges did not result in the defendant being able to create new lending opportunities. Prepayment merely resulted in those prepayment funds coming into Avanti's accounts and becoming part of the excess capacity. There was no link between prepayment and subsequent lending to any new lender.

[21] The Judge held that the safe harbour formula was not suited to the defendant's company structure and its way of doing business. She accepted the expert opinion evidence from a Professor Bowman who was called by Avanti. He deposed that in estimating a creditor's loss, the safe harbour formula implicitly assumed that the lender had no excess capacity and so the prepayment enabled a subsequent new loan to be made. She considered that his evidence demonstrated that where excess capacity exists in relation to an entity with Avanti's structure, a reasonable estimate of loss on prepayment must be seen in the context of there being no lending opportunities created by prepayment. Therefore, mitigation by re-lending was not an option.

[22] She held also that the fact that Avanti's formula did not allow for the reduction of the outstanding balance over the 90 day period, or for the time value of money, had no practical effect on all but one of the outcomes of the 50 loan prepayments. Despite those omissions, Avanti received less under its formula than its actual loss. Avanti's formula did provide a means to reasonably estimate the company's loss. The Judge concluded that a perfect estimate was not required. She concluded that the informant had not satisfied her beyond reasonable doubt that Avanti had calculated an unreasonable estimate of its loss.

The appellant's submissions

[23] It was the essential submission of Mr Woolford for the Commerce Commission that Avanti was required for the purposes of ss 51 and 54 of the CCCF Act to calculate its estimate of loss on the assumption that it would immediately re-lend the funds prepaid at the then prevailing interest rates.

[24] He relied on the safe harbour procedure provided for in s 54(1)(a) of the CCCF Act, as in general terms an indication of what was in fact reasonable. It is not necessary for the purposes of this judgment to set out the relevant rule setting out the safe harbour formula, r 9 of the Credit Contracts and Consumer Finance Regulations 2004. The rule involves the application of a technical and formulaic calculation, the essence of which is that the creditor's loss is calculated on the basis of the difference between the funding rate on the original loan as provided for in the contract and the retail rate prevailing at the break date. Thus it assumes that the funds prepaid can be relent to a new borrower and focuses on any differential in interest rates. The creditor must, therefore, consider what interest rate would be obtained with the same type of loans if the funds were relent for the period remaining on the original credit contract. If interest rates have risen since the original credit contract was made, then once the prepaid funds are relent the creditor who is locked into a funding contract will not make a loss, save for any administrative costs incurred. If interest rates have fallen since the original credit contract was made, then the creditor may have suffered a loss, which under the safe harbour formula is passed on to the debtor.

[25] Drawing from the safe harbour formula, Mr Woolford submitted that the appropriate procedure must:

a) have regard to changes in the prevailing interest rates on loans;

b) allow for mitigation of lost profit through relending on a new loan – in other words, a notional deeming of relending;

c) allow for the fact that the outstanding balance would be reduced over the remaining period of the loan; and

d) make allowance for the time value of money.

He submitted that effectively Avanti had circumvented the mitigation requirements of the safe harbour formula. He did not suggest that the creditor must always use the safe harbour formula. However, he submitted that where, as in this case, the loan otherwise met the criteria necessary for the application of the safe harbour formula, any procedure that is different from the safe harbour formula must nevertheless take into account those fundamental principles. Any alternative procedure must operate in broadly the same way as the safe harbour formula.

[26] Mr Woolford submitted that it was wrong for a creditor to depart from the safe harbour formula for reasons linked to the structure of its business. It was only reasons linked to the characteristics of loans that would be an acceptable basis for departure.

[27] The debate has real implications for Avanti customers. At the time of the prepayments Avanti's prevailing interest rate was the same as that shown in the loan contract. In relation to the transactions to which the 50 charges relate, Avanti would have got no prepayment fee under the safe harbour formula, but it did get a prepayment fee under the formula used in the credit contract.

A purposive interpretation

[28] Section 3 of the CCCF Act sets out its purposes. The first purpose is to protect the interests of consumers in connection with credit contracts. Section 3(g) states that a purpose is to prevent oppressive contracts and oppressive conduct by creditors. Mr Woolford for the Commerce Commission rightly emphasised the consumer protection purpose of the CCCF Act, and it must be taken into account when the specific sections are interpreted.

[29] It is necessary to turn to the words of the sections under which Avanti is charged, ss 51 and 54. The allegation is that in breach of s 51 Avanti required an amount for full prepayment that exceeded a reasonable estimate of its loss arising from full prepayment. The charges under s 54 expressed the same concept in a

different way. The complaint is that Avanti calculated an unreasonable estimate of loss arising from full prepayment contrary to s 54.

[30] The critical word is "reasonable". Although the word is not specifically defined, the concept of "reasonable" or "unreasonable" is amplified in other sections of the CCCF Act by requiring the Court to have regard to certain factors (ss 42, 44). The word "reasonable" in relation to full prepayment fees is used in conjunction with the words "estimate of loss" in s 43, s 51(1)(c) and s 54(1) but without further elaboration as to what "reasonable" means. The Court does not have to have regard to any particular factors in assessing what is a reasonable estimate of loss, although it will bear in mind the consumer protection purpose of the CCCF Act.

[31] Given that purpose, I interpret the phrase "reasonable estimate of loss" as meaning an estimate that on an objective informed analysis at the time of the entering into credit contract will do no more than compensate the creditor for the actual losses it could expect to sustain in the event of prepayment. An estimate of loss calculation will be unreasonable if it will result in a creditor recovering significantly more than its actual loss arising from the prepayment. That would be unfair on a consumer, who would effectively be giving the creditor a bonus payment. Clearly it is the intention of ss 43, 51 and 54 to prohibit a creditor from making extra profit out of prepayments.

[32] However, it is equally clear that the sections contemplate the creditor being able to recover its losses. If the application of the procedure results in a loss calculation and a net figure that does no more than provide some compensation for the creditor's anticipated loss on prepayment, that is not unreasonable. The consumer has made a choice to pay early, and in doing so has to contribute to the lost profit that would have otherwise been enjoyed by the creditor during the agreed duration of the contract. The fact that this is consumer protection legislation does not mean that creditors should accept losses on prepayment. There is no policy reason why a creditor cannot get fair compensation when a consumer chooses to repay the loan early.

[33] Sections 54(1)(a) and (b) are differentiated by the word "or". There is nothing in the words to suggest that (a) and (b) are not true alternatives. One provides for a prescribed formula. The other leaves it up to the creditor to devise a procedure that will give rise to a reasonable estimate of loss. They do not naturally read, as Mr Woolford submits, so that the reasonableness of the creditor's formula must be measured by its similarity to the prescribed formula.

[34] The date at which the reasonableness of the estimate is to be considered is the time of the making of the contract, not the time of the prepayment. This is implicit in the words of s 54(1)(b) which refers to the reasonable estimate being an appropriate procedure "set out in the consumer credit contract". The formula must create an appropriate procedure at the time that credit contract was created. Later events cannot affect reasonableness. Such an approach is consistent with the general approach to the consideration of whether a contractual clause is a penalty (*Dunlop Pneumatic Tyre Company Ltd v New Garage & Motor Company Ltd* [1915] AC 79 at 87), which is to assess the position at the time of the creation of the contract.

[35] The legislature could, of course, have chosen to prohibit any fees or charges being imposed by a creditor on prepayment. That would clearly be in the consumer's interests, but it would have had the effect of providing a great disincentive to creditors to lend at all, or prompt them to lend at higher interest rates, as they endeavoured to guard against the uncompensatable losses resulting from early prepayment. The legislature did not chose this course.

[36] The concept of loss behind the Avanti formula has long been recognised in the common law in relation to breach of contract. The case law on loss on breach of contract and the duty to mitigate loss was the subject of considerable attention during the trial and in the appeal, and is specifically referred to in the statement of the question on appeal. The approach to loss in the common law is relevant to a consideration of reasonable loss under the CCCF Act.

Comparison with the common law

[37] The common law principles that apply where a party suffers from a breach of a contract cannot dictate the answer to the issue, which is essentially a question of the interpretation of ss 51 and 54. However, those cases do reflect a judicial perception of reasonableness. They articulate the concept that a party faced with non performance of a contract is entitled as far as money can do it, to be placed in as good a situation as if the contract had been performed: *British Westinghouse Electric and Manufacturing Co. Ltd v Underground Electric Railways Co. of London Ltd* [1912] AC 673 at 689, *Thompson (W.L.) Ltd v Robinson (Gunmakers) Ltd* [1955] Ch 177 at 183. A prepayment is not a breach of contract, but the common law principles were not designed to penalise a party in the wrong, but to compensate for actual loss.

[38] It is equally an established principle that in assessing loss, where there is a loss of a business opportunity such as a sale of a car, and where supply exceeds demand, then the benefit of the opportunity or sale must be regarded as lost. The position is clearly set out in Trietel *The Law of Contract* (12 ed 2007) at para 20-099:

> The injured party is, however, required to mitigate in this way only if the new transaction would be a true substitute for the old one. Where, for example, a customer wrongfully repudiates a contract for the provision of services at a time when the injured party has spare capacity, then the possibility of that party's making another contract with a new customer will not be taken into account: such a new contract will not be a true substitute for the broken contract since the injured party would, but for the breach, have been able to perform both contracts.

This principle is referred to in a number of leading cases including *Re Vic Mill* [1913] 1 Ch 465 (CA) p 473; *Thompson (W.L.) Ltd v Robinson (Gunmakers) Ltd* [1955] Ch 177, 187; *Interoffice Telephones Ltd v Robert Freeman Co. Ltd* [1958] 1 QB 190 (CA) at 195-201; and *Robophone Facilities Ltd v Blank* [1966] 1 WLR 1428 at 1442-1443.

[39] Mr Woolford sought to rely on a statement by Lord Denning MR in *Lazenby Garages Ltd v Wright* [1976] 1 WLR 459, where there was a sale of a used car, and default by the buyer. The car was resold. Lord Denning at p 462 set out the general principle:

> The cases show that if there are a number of new cars, all exactly of the same kind, available for sale, and the dealers can prove that they sold one car less than they otherwise would have done, they would be entitled to damages amounting to their loss of profit on the one car.

However, Lord Denning MR went on to state that because the case on appeal involved a used car, it could not have been in the reasonable contemplation of the buyer that there would be an available market for that car. At most what would have been contemplated would have been a resale of the same car to a new buyer but at a lower price. Given the fact that the car had been sold for more than the original purchase price in that case, there was no damage. It was this part of the judgment that Mr Woolford relied on.

[40] I do not consider that this case assists the Commerce Commission's argument. Indeed, to the contrary, it supports the proposition that the contracting party is entitled to be compensated for the loss of profit on a sale in the event of default, where supply exceeds demand and no replacement sale can be made to mitigate the loss. Avanti was in a position where its supply of funds for lending exceeded demand. When prepayment occurred, Avanti had one loan less than it otherwise would have had. It therefore lost the profit on that loan. There could be no onlending of the funds in the sense of the loss being mitigated by a new loan contract. The new contract would have been enjoyed by Avanti in any event because it had funds available for all customers.

[41] The analysis shows that the premise upon which the Avanti formula was based was a reasonable premise. It is in accord with common law principles developed over the years relating to the assessment of loss. It assists in the interpretation of the alternatives in s 54(1).

Application of the safe harbour formula

[42] Mr Woolford's submission was that the alternative "appropriate procedure" provided for in s 54(1)(b) had to have the various features evinced in the safe harbour formula, particularly in this case, a calculation based on the contract and current market interest rate differential. It is this submission which lead to the core question in the case on appeal of whether the alternative "appropriate procedure"

must involve a calculation which assumes the immediate relending of the funds at the then prevailing interest rates, as provided for in the safe harbour formula.

[43] It makes no logical sense for the legislature to have provided two alternative methods for the calculation of a reasonable estimate of loss, but to have one essentially driven by the terms of the other. If that had been the legislature's intention, it could have been expected that it would have said so, rather than to provide what is on its face a clear alternative.

[44] The legislature chose to allow the creditor to be compensated for actual losses arising from early prepayment. The only benchmark is reasonableness. It is perfectly reasonable for a loss to take into account the fact that a new loan will not replace the old, and that the profit on a loan is lost through prepayment. The loss of the benefit of the profit on the loan is as real as any other sort of contractual loss. The safe harbour formula does not contemplate an excess of supply over demand. It presupposes that the creditor will be able to enter into a replacement contract with a new customer and thereby suffer no loss at all if the interest rate remains the same, and at worst will only suffer the loss of the differential interest rates. However, as the cases show, this is not always a fair test of loss.

[45] The reasonableness of this interpretation of s 54(1) can be demonstrated by applying the safe harbour formula to the current market situation. It was common ground in submissions from the bar that at the present time with existing depressed interest rates, Avanti would in fact be better off in relation to a prepayment using the safe harbour formula. The Avanti prepayment formula is based on the differential between the calculated cost of funds, and the market interest rate, and only over a limited 90 day period. Avanti would be better off using the safe harbour formula based on the differential for the term of the contract between the interest rate in the contract and the now much lower market interest rate. It must be born in mind, as the learned Judge observed, that a reasonable estimate does not require a perfect estimate. Indeed, given the big variations in market conditions, a perfect estimate in the sense of a formula which will always lead to a calculation of the exact loss is impossible. Such a formula cannot be devised.

[46] It might be said that the safe harbour formula is unlikely to be adopted by any finance companies as every prudent finance company will have some excess capacity. However, events in the market would indicate that many finance companies have not had excess capacity in recent times. Moreover, some companies may fund themselves solely on the basis of shareholders' funds or debentures, and may be in a position at times where they do not have excess capacity. Even if the submission was right and the safe harbour formula would be unappealing to all properly run finance companies, that is not a reason to negate the plain meaning of the alternative in s 54(1)(b).

[47] There were benefits to the consumer in the prepayment formula used by Avanti. In addition to the formula not compensating Avanti for drastic drops in the market interest rate, it also treated the prepayment as if it was immediately paid to Avanti's bank to offset the interest charge. Further, the calculation of loss ran for only 90 days. If much more the 90 days was still to run, the amount payable remained the same, to the consumer's benefit. If the amount to run was 90 days or less, that actual duration was used to apply the formula. This seems to be entirely fair.

[48] Even though this is consumer protection legislation, the purposive interpretation cannot extend to rewriting a text in a way which does violence to the plain words: *CIR v Auckland Harbour Board* [2001] 3 NZLR 289 at 299. In any event, such efforts are not required, as there is nothing intrinsically unfair to the consumer in a formula which presupposes supply exceeding demand.

[49] In the circumstances the District Court Judge was quite right to describe the Avanti formula as conservative and one which produced a fee less than its estimate of loss.

Penalty

[50] Mr Woolford argued that the prepayment clause was a penalty, relying on the definition of a penalty set out in *Dunlop Pneumatic Tyre Company Ltd v New Garage & Motor Company Ltd* [1915] AC 79. In that case a distinction was drawn

between a contract which contained a genuine pre-estimate of loss, against a penalty which is a payment of money stipulated as "in terrorem of the offending party" (p 86).

[51] For the reasons set out, the clause here did not provide for a payment in terrorem. Rather, it was a formula designed to calculate a reasonable estimate of actual loss. Therefore, the prepayment clause was not a penalty.

Further submissions of appellant

[52] I cannot accept Mr Woolford's submission that it is not appropriate to look at the circumstances of the company set-up, but only to look at the terms of the loan. An assessment of reasonableness requires more than just a barren focus on a contractual term against a market backdrop. Section 54 is headed "Creditor's loss arising from full prepayment" and states that what is to be calculated by a creditor is a reasonable estimate of "its" loss, not of some notional or hypothetical creditor. This is the same as the approach of the Courts in the common law mitigation cases. If a rigid formula was to be applied, there would have been no need for the alternative in s 54(1)(b).

[53] Mr Woolford submitted that the District Court Judge wrongly considered the matter at the time of prepayment. However, it is quite clear that the Judge did not make this mistake. She considered whether the actual formula calculated a reasonable estimate of loss on the basis of the excess capacity that Avanti had at the time of the contract.

[54] Mr Woolford also argued that the question of the capacity of the lender cannot be determinative as all finance companies that are prudent have excess funds and the debtor does not know the circumstances of the creditor. However, as already mentioned, the plain words of s 54(1) require a reasonable estimate of the particular creditor's actual loss. The fact that the debtor may not know those circumstances is not an answer, because the debtor, of course, always has the option of not proceeding with the contract when faced with such a term, or not prepaying.

Conclusion

[55] I consider, therefore, that the answer to the question for the opinion of the Court is "no". The defendant was not required for the purposes of ss 51 and 54 of the CCCF Act to calculate a reasonable estimate of its loss on the assumption that it will immediately lend the funds prepaid at the then prevailing interest rates, even when it has excess lending capacity. As the Judge found, if there is excess lending capacity, then a reasonable estimate does not require the assumption that funds will immediately be re-lent, and here Avanti did have such excess lending capacity.

Result

[56] The answer to the question in the appeal by way of case stated is no. The appeal is dismissed.

Costs

[57] On the face of it costs are payable by the Commerce Commission to Avanti on a 2B basis. I have been asked to reserve costs. If the parties cannot agree, Avanti should file submissions on the question of costs within 7 days, and the Commerce Commission within a further 7 days.

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Asher J