IN THE COURT OF APPEAL OF NEW ZEALAND

CA727/2013
CA593/2014
[2015] NZCA 78

BETWEEN	SPORTZONE MOTORCYCLES LIMITED (IN LIQUIDATION) First Appellant
AND	MOTOR TRADE FINANCES LIMITED Second Appellant
AND	COMMERCE COMMISSION Respondent

Hearing:	19–20 November 2014 (further submissions received 12 December 2014)
Court:	Harrison, Stevens and Simon France JJ
Counsel:	D J Goddard QC, I J Thain and C M Moody for First and Second Appellants S J Mills QC and K C Francis for Respondent
Judgment:	30 March 2015 at 11.30 am

JUDGMENT OF THE COURT

A The appeal is dismissed.

B The appellants must pay the respondent costs for a complex appeal on a band B basis and usual disbursements. We certify for second counsel.

REASONS OF THE COURT

(Given by Stevens J)

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Unreasonable fees?

[1] This appeal concerns fees (establishment fees, default fees and other credit fees) charged by the appellants to consumers through consumer credit contracts governed by the Credit Contracts and Consumer Finance Act 2003 (CCCFA). The appellants, Sportzone Motorcycles Ltd (in liq) (Sportzone) and Motor Trade Finances Ltd (MTF), appeal from findings in the Auckland High Court that certain fees provided for in credit contracts entered into by Sportzone with borrowers were unreasonable for the purposes of the CCCFA.[1] These findings are set out in two

[1] Sportzone has since been placed in liquidation and the liquidators have given their consent to the continuation of this proceeding against Sportzone.

judgments of Toogood J, the first dealing with liability, the second with quantum (referred to as the liability judgment and the quantum judgment, respectively).[2]

[2] The findings and conclusions in both the liability and quantum judgments are challenged.[3] The substance of this appeal is largely a matter of interpretation of the relevant statutory provisions. We approach this interpretative exercise with an eye to the policy apparent from the text of the CCCFA and its underlying purpose as an important consumer protection measure.

[3] The appellants reject what they call the High Court's "fine-grained costs-based approach" to determining whether a fee is unreasonable under s 41 of the CCCFA. They argue the High Court wrongly accepted the approach contended for by the Commerce Commission (the Commission), which is inconsistent with the text and purpose of ss 41, 42 and 44, and the scheme and purpose of the CCCFA broadly. They contend the approach accepted is unworkable in practice; produces results that are of little or no practical use to debtors; discourages innovation and efficiency and is unfair to creditors.

[4] The appellants accept fees under the CCCFA must not be unreasonable. In some provisions, specific activities in relation to which fees can be charged are listed, and only costs incurred in connection with those activities are recoverable. In other provisions, costs must be incurred in relation to general activities falling within a given statutory definition. The present dispute concerns the assessment of when a cost is incurred "in connection with" or "in relation to" an activity and whether that is reasonable.

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2 *Commerce Commission v Sportzone Motorcycles Ltd (in liq)* [2013] NZHC 2531, [2014] 3 NZLR 355 [liability judgment]; *Commerce Commission v Sportzone Motorcycles Ltd (in liq)* (No 2) [2014] NZHC 2486 [quantum judgment].

3 A cross-appeal by the Commerce Commission was also filed, challenging Toogood J's findings in the liability judgment as to alleged breaches of the Fair Trading Act 1986, s 9. This was abandoned in late October 2014. There was no mention of costs arising from this abandonment. We note also that negotiations as to costs arising from the High Court decisions are still on foot. In light of our decision on the costs issues relating to the appeal broadly (see later at [123] onwards), we make no order as to costs on the abandonment.

The competing cases

Core case for Sportzone/MTF

[5] The key proposition for the appellants is that s 41 requires the Court to assess the reasonableness of the various fees charged in a broad commonsense manner. This should be informed, but not determined by, a consideration of actual costs. Fees need not match costs dollar for dollar. The Court should exercise its judgment and it is not required to (nor should it) carry out a detailed cost accounting exercise.

[6] Mr Goddard QC argued the costs to be considered in assessing whether fees charged are reasonable include all costs connected with the matter in question, whether variable or fixed, and whether direct or indirect. There is no warrant for excluding some costs merely because the connection to the fee and the fee activity is not close or direct. The nature of the cost, and the nature of the connection between the cost and the matter giving rise to the fee, may be relevant to the overall reasonableness assessment. But the High Court judgments' interpretation of reasonableness used s 41 in a manner for which there is no statutory basis. The appellants contend, relying on the words of Lord Mustill, that this is an attempt to redefine the word by "thrusting on it a spurious degree of precision".[4]

[7] The appellants' proposition is: if a fee does no more than recover reasonable costs associated with an activity relevant to the basis for the fee, that fee cannot be unreasonable. Pointing to the wording of s 42 in relation to establishment fees, Mr Goddard submitted the Court must consider whether an establishment fee is "equal to or less than the creditor's reasonable costs in connection with the application for credit".[5] However, he argued the converse is not a mandatory consideration: a fee may be reasonable, even though it is not equal to or is indeed more than the costs incurred in connection with the activity to which the fee relates. Thus, direct cost recovery is a "safe harbour", a potential guide to setting reasonable fees, but not a statutory necessity.

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4 *R v Monopolies and Mergers Commission ex parte South Yorkshire Transport Ltd* [1993] 1 WLR 23 (HL) at 29.

5 CCCFA, s 42(a).

[8] The appellants submitted that when assessing whether a fee is reasonable, the Court must also take into account:

(a) other mandatory factors such as reasonable standards of commercial practice;[6] and

(b) any other matters that shed light on the reasonableness of the fee charged.

[9] The core premise of the appellants' case is that anything logically capable of informing or illuminating the reasonableness of the fee should be included. To that end, for example, a comparison with fees charged by other similar lenders would often be a relevant factor.

Commission's response

[10] Mr Mills QC, counsel for the Commission, characterised this proposed interpretation of the relevant provisions as merely requiring a vague link between the cost and the fee charged to the borrower, with the key focus on identifying only "outlier" fees, being fees that are clearly unreasonable. On that basis, any fee a creditor might charge, benchmarked against other lenders, could be reasonable. Mr Mills submitted this approach had the effect of converting the test for unreasonableness in s 41 to one prohibiting only fees that "no reasonable lender could adopt". This interpretation would mean ss 41–44 of the CCCFA would have little, if any, independent role in the statutory scheme.[7]

Issues on appeal

[11] At the heart of this appeal is the nature and extent of the matching required by the CCCFA between fees charged by a lender and the costs to the creditor of performing the relevant fee-related activity. Does the CCCFA permit a creditor to

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6 These "other mandatory factors" are mandatory by virtue of reference to external standards in other provisions of the CCCFA, specifically s 44(1)(b), in relation to other credit fees and default fees. These mandatory factors are not included in s 42.

7 On this analysis the test would essentially collapse down into a mirror of the "oppressive" contracts test, which is tested by reference to "reasonable standards of commercial practice": CCCFA, s 118.

recover all (or virtually all) of its costs as fees, as long as the cost in some way benefits the lending business? Or, does it require the cost to be more closely connected to the relevant cost object?

[12] Breaking down this general question, the parties were in broad agreement that the following are the issues to be determined:

(a) What is the test for assessing whether a fee is unreasonable under s 41 of the CCCFA?

(b) Were the fees charged by Sportzone/MTF unreasonable under s 41 of the CCCFA?

(c) If any of the fees were unreasonable under s 41, is relief available under s 94 to recover the portions of the fees held to be unreasonable, or is relief available only under s 41?

(d) If relief is available under s 94(1)(b), was it established that any borrower had suffered loss recoverable under that provision?

(e) Does s 45, addressing fees passed on by a creditor, assist the appellants in terms of who is responsible for that portion of the fee passed on by MTF to Sportzone?

(f) If relief is available, and if loss has been suffered by any borrower, what is the quantum of that loss?

Background

[13] The key facts are summarised by Toogood J in the liability judgment and we draw on that summary.[8] At the relevant time, during 2006–2008, Sportzone carried on the business of motorcycle sales, servicing and repairs. Sportzone offered financial services to customers who purchased motorcycles.

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[8] Liability Judgment, above n 2, at [6]–[13].

[14] MTF itself provides financial services to the customers of its associated dealers. Sportzone is one such dealer. An associated company, MTF Securities Ltd (MTFS), provided finance to MTF by purchasing its loans, which were then securitised and sold as debt securities on the Euro-Commercial Paper market.[9] Sportzone was a shareholder in MTF, a cooperative company, with its shares owned exclusively by motor vehicle dealers.

[15] Sportzone entered into 39 specific loan transactions, in each providing finance for customers to purchase one of its motorcycles. Each customer borrowed from Sportzone and granted to it a security interest in the motorcycle purchased. Sportzone borrowed funds from MTF to advance the loans to its customers, and its interests in the loan were then assigned to MTF, which in turn sold them to MTFS. Loan repayments by the customers were made directly to MTFS, which used those repayments to make its payments due on the debt securities it had issued and to meet the costs of its programme. Any surplus was paid to MTF, whose only business was that of making and managing loans of this kind.

[16] The terms of each loan from Sportzone provided for the customer to pay certain fees. These included the fees at issue on appeal: an establishment fee and an account maintenance fee charged by Sportzone, an establishment fee and monthly account maintenance fee charged by MTF and a pre-possession fee and repossession fee, charged by MTF in the event of payment default. The MTF fees were charged to Sportzone, which passed them on to borrowers.

[17] The amounts of these various fees provided for in the 39 agreements were set out in schedules to the pleadings and are agreed between the parties. An establishment fee of $190 and $200 was charged by MTF and Sportzone respectively and a monthly account maintenance fee of $3 and $5 respectively was applied to each account. Generally prepossession fees of between $50 and $80, and repossession fees of between $70 and $80 were charged. These loan agreements were entered into between 26 May 2005 and 16 July 2008. They comprise 39 of approximately 100,000 consumer credit contracts entered into by MTF's motor

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[9] MTFS was the third defendant in the High Court proceeding. It is not a party to this appeal.

vehicle dealer shareholders in the years after the CCCFA came into force on 1 April 2005.

[18] It seems MTF had reviewed and changed its loan pricing in the light of the introduction of the CCCFA. Following this review, MTF altered its fee structure to recover a greater proportion of its operating costs through fees. MTF claimed that its fees still did not cover all of its operating costs and any increase in fees was matched by a reduction in MTF's lending interest rate margin. Dealers passed on an even greater reduction in interest rate margin to their customers. MTF gave evidence its increased fee income did not lead to increased profits. It contends the amount of each of its fees was in line with the amounts charged by competing lenders.

Commission's intervention

[19] In response to a complaint in August 2006 the Commission commenced an investigation into Sportzone. The investigation identified evidence that raised significant concerns regarding Sportzone and MTF's general approach to compliance with the CCCFA.

[20] In the High Court it was common ground that Sportzone, MTF and MTFS were "creditors" as defined in the CCCFA.[10] The central focus of the case was the cost analysis carried out by the appellants in an effort to show the required connection between their costs and rate of establishment, credit and default fees charged. Sportzone's allocations were relatively simple; MTF's allocations were highly complex. Mr Mills submitted this complexity was largely the result of MTF's decision to recover virtually all of its costs through one or more of its fees: Sportzone/MTF had adopted a practice of drawing increasingly tenuous connections between overhead and other indirect fixed costs and using those to justify its fees.

[21] MTF used a full cost-absorption model, in which the only cost excluded from recovery through fees was the cost of funds, the cost of its securitisation programme

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[10] CCCFA, s 5.

and the cost of capital.[11] It divided its expenses into a number of separate "cost centres" (such as finance, treasury, credit, managing director, sales management). The budget for each cost centre contained a number of cost categories and line items. For each financial year, MTF undertook a separate allocation of each line item to one or more of the four different fee categories it was using, namely establishment, maintenance, pre-payment and default fees. The costs for each category were then divided by the estimated number of fees MTF expected to charge in the next 12-month period (for example, the number of loan contracts it would enter into). They were then compared to existing or proposed fees.

[22] It seems from the evidence before the High Court, the MTF board treated the introduction of the CCCFA as presenting "profit opportunities" including the chance to "boost fee income". The Commission contended the evidence showed that there was some discomfort, even within MTF, at this aggressive approach to recovering costs through fees. One of MTF's senior executives commented that any attempt to claw back provisions and bad debts through fees "would be wrong". Nevertheless MTF sought to recover, and is still seeking to recover before this Court, such items through fees.

The statutory scheme

[23] The CCCFA is the centrepiece of the legislative framework regulating consumer credit transactions. It replaced the Hire Purchase Act 1971 and the Credit Contracts Act 1981. The purposes of the CCCFA are set out in s 3:

> **The purposes of this Act are**–
>
> (a) to protect the interests of consumers in connection with credit contracts, consumer leases, and buy-back transactions of land; and
>
> (b) to provide for the disclosure of adequate information to consumers under consumer credit contracts and consumer leases–
>
> (i) to enable consumers to distinguish between competing credit arrangements or competing lease arrangements; and

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[11] Being the cost of funds used to finance its business — in MTF's case, what it considered its shareholders required as an acceptable rate of return in order to stay invested in business: quantum judgment, above n 2, at [90].

(ii) to enable consumers to become informed of the terms of consumer credit contracts or consumer leases before they become irrevocably committed to them; and

(iii) to enable consumers to monitor the performance of consumer credit contracts or consumer leases; and

(c) to provide rules about interest charges, fees, and payments in relation to consumer credit contracts;

…

[24] As Mr Goddard submitted, paragraph (c) is most directly relevant to the provisions in issue in these proceedings. Yet it provides no guidance on the rules in the CCCFA about fees. Paragraph (a) provides some guidance at a very general level, leaving it to the court to identify how the rules in question should operate in order to protect the interests of consumers. Paragraph (b) underscores the importance of disclosure of information to consumers, but sheds no light on the substantive constraints on fees imposed by the Act.

[25] Part 2 governs consumer credit contracts.[12] A consumer credit contract is defined as a credit contract where the debtor is a natural person who enters into the contract primarily for personal, domestic or household purposes, and certain other prescribed situations.[13] Subpart 2 provides for the required disclosure of a creditor under a consumer credit contract in relation to certain matters.[14] Section 17, for example, provides for initial disclosure, which must be made before the contract is entered into or within five working days of it being made.[15]

[26] Sections 18–21 set out the requirement for continuing disclosure and its mandatory contents.[16] Additionally, variations to consumer credit contracts must be disclosed to the debtor and further disclosures must be provided upon request from a debtor.[17]

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12 Section 10.
13 Section 11.
14 Sections 17–26.
15 Section 17 also requires that all the relevant key information set out in sch 1 to the CCCFA must be disclosed in that initial disclosure statement: s 17(1).
16 Including, for example, disclosure of all fees and charges debited to the debtor's account during each statement period: s 19(f).
17 Sections 22–24.

[27] Subpart 3 establishes the circumstances giving rise to the debtor's right to cancel. Subpart 4 provides for standards of disclosure. Subpart 5 deals with interest charges. It ensures that the contract specifies the annual interest rate applicable under the contract, and that interest is (generally) charged in arrears on the outstanding balance of the credit provided. Although subpart 5 regulates interest and default interest charges, it does not impose any restrictions on the rate of interest that may be charged under a consumer credit contract.[18]

[28] Subpart 6 is central to these proceedings and concerns fees payable under consumer credit contracts. The prohibition on unreasonable fees is found in s 41, which provides:

> **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.
>
> (3) The court may make any other order it thinks fit for the purpose of giving effect to an order under subsection (2).
>
> (4) An application for an order may be made within 1 year of the day that the fee is imposed or debited under the consumer credit contract.

Establishment fees

[29] The term "establishment fees" is defined as follows:[19]

> **establishment fees** means the fees or charges payable under the credit contract that relate to the costs incurred by the creditor in connection with *the* application for credit, processing and considering *that* application, documenting *the* contract, and advancing *the* credit; but does not include any fee or charge to the extent that it is a charge for an optional service

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[18] It does, however, set out the procedure for reopening a credit contract. An interest rate that is considered "oppressive" under the provisions in subpart 5 would be liable to being reopened and relief granted. The requirement an interest rate not be oppressive is the only overarching restriction on interest rates: s 120. This reflects the "light touch" regime applicable to interest, which is limited to ensuring full disclosure and preventing interest from being charged in advance: see ss 36–40.

[19] Section 5 (emphasis in italics added).

[30] Section 42 focuses specifically on costs recoverable as fees in relation to establishment activities:

> **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.
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> (Our emphasis).

Other credit and default fees

[31] Both credit fees and default fees are defined in the CCCFA:[20]

> **credit fees** means fees or charges payable by the debtor under a credit contract, or payable by the debtor to, or for the benefit of, the creditor in connection with a credit contract (including any insurance premiums payable if the creditor requires the debtor to obtain insurance cover from a particular insurer); but does not include the following:
>
> (a) interest charges:
>
> (b) a charge for an optional service:
>
> (c) a default fee or default interest charge:
>
> (d) government charges, duties, taxes, or levies:
>
> …
>
> **default fees** means fees or charges payable on a breach of a credit contract by a debtor or on the enforcement of a credit contract by a creditor; but does not include default interest charges

[32] Section 44 sets out the relevant criteria for determining the reasonableness of other credit or default fees. It provides:

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[20] Section 5.

> **44 Other credit fees and default fee**
>
> (1) In determining whether a credit fee or a default fee is reasonable, the court must have regard to,–
>
> (a) in relation to the matter giving rise to the fee, whether the fee reasonably compensates the creditor for the following:
>
> (i) any cost incurred by the creditor (including the cost of providing a service to the debtor if the fee relates to the provision of a service):
>
> (ii) a reasonable estimate of any loss incurred by the creditor as a result of the debtor's acts or omissions; and
>
> (b) reasonable standards of commercial practice:
>
> (2) This section does not apply to–
>
> (a) establishment fees; or
>
> (b) a fee or charge payable on a part prepayment under a consumer credit contract; or
>
> (c) a fee or charge payable on a full prepayment of a consumer credit contract (unless the fee relates to the administrative costs).

[33] Section 44(2) makes it clear s 44 does not apply to establishment or prepayment fees. This section is constructed differently from s 42; we return later to the focus of this section, which we consider explains this different structure.

Liability judgment

[34] The High Court accepted the Commission's approach to the interpretation of the term "unreasonable fees" in s 41. Toogood J held a fee is unreasonable except to the extent that it recovers costs of the kind set out in s 42 or 44 of the CCCFA.[21] The recoverable costs referred to in those provisions are costs that are closely relevant to the matters or activity in respect of which the fee is charged. The Judge identified the matters listed in ss 42 and 44 as "mandatory but not necessarily exclusive criteria" for determining whether a fee is unreasonable.[22] The Judge did not consider any other factors as relevant to the determination of reasonableness.

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21 Liability judgment, above n 2, at [67].

22 At [18] and [20].

[35] The Judge undertook a careful assessment of the costs listed as being recovered by the fees charged. Toogood J framed the central question for his determination as follows:

> [29] The central question is essentially one of statutory interpretation: are the expressions "in connection with" in s 42(a) of the CCCFA, and "in relation to" in s 44(1)(a), to be read narrowly so as to limit costs recoverable by fees to variable costs and some directly-related fixed costs determined by reference to the activities involved in a particular transaction? Or should those provisions be applied broadly so that any direct or indirect costs having some beneficial relationship with the particular activity concerned, whether they are variable costs or fixed costs associated with the business of lending, are recoverable by fees?

[36] The Judge rejected the views of the appellants' expert witnesses: that there is a connection between a cost and an activity in respect of which a fee is charged for the purposes of ss 42 and 44 if there is a beneficial relationship between that cost and activity. This is apparent from the Judge's conclusions as follows:

> [35] Two features of the inquiry under s 42 should be noted. First, the use of the definite article in referring to "the application for credit" reinforces the inference to be drawn from the use of the term "an" establishment fee at the beginning of the section, that the Court's inquiry is directed not to whether the lender's fees in general are reasonable, but whether an establishment fee charged in a particular transaction is unreasonable. This is implied also by the definite article directing the Court to consider "the amount of the fee".
>
> [36] Further, the three chronological steps following the application for credit are referable to the particular transaction; namely, processing and considering "that" application, documenting "the" consumer credit contract, and advancing "the" credit.
>
> [37] The second notable feature of the inquiry is that it is process oriented. What must be assessed is the reasonableness of the costs in connection with the four chronologically-listed steps taken when a credit application is made and granted. That implies that it may not be reasonable to charge an establishment fee which recovers costs which are remote from individual transactions and are connected more closely with the general overheads of the business; that is, costs not directly attributable to the four steps. Even where an average reasonable costs approach is taken under s 42(b), the question remains how the fee charged for the particular transaction compares to the creditor's average reasonable cost for each of the four steps identified in the paragraph.

[37] The Judge preferred instead the Commission's argument that the inquiry under ss 42 and 44 is transaction specific.[23] The costs considered must be those related to the credit transaction and not the sale and purchase transaction (or the business of selling) in general. The Judge also observed s 42 required the determination of reasonableness to be made in respect of a particular case or loan, because the nature of the remedies for any breach of obligation under s 41 are necessarily fact or transaction specific.[24]

[38] The different wording used in s 42(a) and s 44(1)(a), was attributable only to the structure of inquiry required by each, and did not affect the standard of connection required for the different categories of costs. Accordingly, the Judge found the required degree of connection to be the same for each of ss 42, 43 and 44.[25]

[39] The Judge then assessed the listed statutory purposes of the CCCFA.[26] With specific reference to ss 41–44, he considered the operative purposes guiding his interpretive exercise as: (i) consumer protection; (ii) the provision of adequate information; (iii) identifying the circumstances in which fees can be charged and the levels of them; and (iv) assisting the enforcement of lender obligations.[27] In terms of the concept of reasonableness Toogood J said:

> [65] I am not persuaded that it is necessary to read words into the statute in order to give effect to which I consider to be the meaning provided by the text in the light of the relevant statutory purposes. The overriding consideration is that of reasonableness contained in s 41. Reasonableness is to be judged from the view of an informed objective bystander considering whether it is reasonable for the particular borrower to meet the costs which the lender seeks to recover by the fees charged. That exercise is not assisted by a test which, in effect, permits a creditor to justify any fee on the basis that it is simply recovering an actual business cost incurred by the creditor, other than the cost of the funds advanced, no matter how remote the cost may be from the transaction in which the fee is charged.

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23 At [38].

24 At [39]. The Judge referred by way of example to applications under s 93 of the exercise of the Court's power to make orders under s 94(1)(b) for compensation for loss or damage.

25 At [44]–[45]. The different expressions to which Toogood J is referring are "in connection with" in subs 42(a), "arising from" in subs 43(1) and (2) and "in relation to" in subs 44(1)(a).

26 Section 3.

27 At [63]–[65]. In reaching this conclusion, Toogood J drew on the legislative history of the CCCFA and the guidance as to policy that offered (admissible as per *Skycity Auckland Ltd v Gambling Commission* [2007] NZCA 407, [2008] 2 NZLR 182 at [39]–[42] and *Tiny Intelligence Ltd v Resport Ltd* [2008] NZCA 281, [2009] 1 NZLR 590).

> [66] … To be reasonable, the cost the creditor seeks to recover must be sufficiently close and relevant to the establishment of the particular loan, to the administration and maintenance of the particular loan, or to the actual consequences of the particular default, such that it can reasonably be said that the cost was incurred in connection with or in relation to the relevant matter.

[40] The Judge acknowledged this did not provide a "bright line test".[28] At the margins, it will be a matter for judgement in the particular circumstances whether there is a sufficiently close and relevant connection between the fee charged and the cost claimed in respect of it.

[41] The parties each called expert accountancy evidence to assist the Court in applying the test adopted.[29] The Judge concluded the most effective approach was "the variable cost approach advocated by Professor Robert Bowman, or a variation of it".[30] The evidence of a forensic accountant, Mr John Cregten, offered the slight variation on the approach of Professor Bowman, allowing recovery of some fixed costs, that could be established to meet the close relevance test.[31] The Judge noted:[32]

> … Mr Cregten's thorough analysis has persuaded the defendants that, if the Commission's approach to the central issue is favoured by the Court, they cannot realistically take issue with his conclusion that the fees charged were unreasonable in terms of the statute. Nor do they dispute most of the amounts by which he assesses the borrowers have been overcharged. Where Mr Cregten has quite properly suggested a range of fees which he would regard as reasonable for any activity or matter, the Commission is content to take the higher figure as that which should be applied.

[42] The Judge was also assisted by the evidence of Robert Smith, another expert witness for the Commission. Mr Smith was a former Chief Executive Officer and Director of the Southern Cross Building Society, who presented a process for assessing the appropriateness of establishment and other fees, which was found to provide "general guidance to the close relevance approach which the Act calls for whatever the nature of the lending activity".[33] Toogood J added:

> [86] First, the employer should assess the time taken by the responsible employee or employees to consider, process and document each loan.

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28 At [68].
29 At [82].
30 At [83]. Professor Bowman was called by the Commission.
31 At [84].
32 At [83].
33 At [85].

> Plainly an averaging approach to the assessment would be appropriate for the purpose of setting fees even though individual cases might involve more or less time than the average. Second, an allocation of the employer's total cost of remuneration (including salary and other benefits) should be undertaken. Third, allocating the total cost of remuneration to the time taken to establish the loan would provide an indicative range for the fee.
>
> [87] In an appropriate case, it might be reasonable to add other variable costs having a causal link to the establishment of the loan, and fixed direct costs other than employee remuneration which may include IT costs properly referable to the establishment activities.

[43] In the liability judgment the Judge did not quantify the amount by which he considered the relevant fees were unreasonable. Rather he reserved the matter for discussion between the parties and further submissions. This process led to the quantum judgment. We discuss that decision further when addressing the issues of relief and loss.[34]

The test under s 41 - did the appellant charge unreasonable fees?

Submissions of the parties

(i) Sportzone/MTF

[44] In respect of establishment fees, Mr Goddard argued the inquiry under s 42(a) into the costs incurred in respect of the four particular aspects of the credit contract transaction set out in that paragraph is simply the first step. But then, a broader inquiry is still required. A creditor is not required to undertake a careful allocation exercise, tying all potential costs to the four identified activities in s 42. The appellants resist the characterisation that every dollar charged must be referable to a particular cost in respect of the activity for which it is charged. Rather, if a fee does no more than recover reasonable costs associated with one of those activities, it is clearly reasonable. The court must step back and assess costs holistically.

[45] Unreasonableness under ss 41 and 42 is accordingly not determined by a costs inquiry alone. While the concept of reasonableness must have some tangible content, it is wrong to narrow it solely to costs actually incurred and clearly referable to an identifiably relevant activity. Rather, the statutory direction to have regard to

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[34] See at [114]–[121] of this decision.

whether the amount of the fee is equal to or less than the creditor's reasonable costs amounts to a "safe harbour". If the fee is of that type, namely squarely referable to costs, the inquiry ends there. But if not, the inquiry becomes an exercise in overall judgment, retaining a "margin of appreciation" for relevant costs, determined by a range of factors capable of illuminating the inquiry, namely:[35]

(a) a comparison of the fees charged by others in the same industry (Sportzone/MTF draw support for this factor from the inclusion of reference to reasonable commercial standards in s 44 and other provisions);

(b) the background to the fees and any adjustments made to take into account history (including, for example, no history of over-recovery or other investments in the activity in question);

(c) any mismatch between recoverable costs and the fees and whether they were increased without a proper cost justification; and

(d) the transparency of the fee.

[46] Accordingly, Mr Goddard contends the approach adopted by the High Court, amounting to a requirement for a direct connection between cost and fee, is wrong. Imposing the test of close relevance is a gloss on the provisions and is artificial, unfair and an unwarranted restriction on the factors properly to be taken into account. Rather, reasonableness should be assessed in a broad, common sense manner. The nature of the cost and closeness of connection to the activity may be a relevant factor in the overall assessment – but no close connection is required. Any cost connected with the matter or activity in respect of which a fee is charged is relevant, guided at all times by logic and common sense. The requirement is simply for a reasonable allocation of fees. This is true for both ss 42 and 44 alike – Mr Goddard contends the broad inquiry mandated by s 41 imports this holistic assessment for all fees, regardless of which statutory provision they are governed by.

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[35] These are said to be the factors that assist a "holistic" assessment of reasonableness.

[47] Mr Goddard submitted there was no necessity for exact correspondence between costs and fees. All costs incurred will always be relevant. He accepted that MTF could not attribute 100 per cent of managing director's costs to establishment fees. A degree of sensibility, but not necessarily exactitude, is required in determining how much of a cost is attributable to a particular activity. Further, there is no magic in the beneficial relationship test. The better approach is to ask whether what has been paid or expended in costs contributed to the company's performance of the activity, whether directly or indirectly. If it did, it ought to be caught by ss 42 or 44. And so, most of MTF's costs were connected with the various activities because none of the lending would happen without the input of the costs identified.

[48] Mr Goddard contended the CCCFA overall, with its objective of consumer protection, mandates a light-handed approach in line with his submission. This approach is most consistent with the goal of promoting creditor innovation, efficiency and flexibility.

(ii) Commission's response

[49] Mr Mills responded as follows:

(a) The Sportzone/MTF argument was creditor, not borrower, focussed and essentially resulted in self-regulation of fees by the industry. On the contrary, the purpose of the CCCFA was to introduce the Commission as regulator. The argument advocating the use of "benchmarking" fees to those charged by other lenders deprives the relevant provision of its true purpose, making the CCCFA incapable of or undermining its power to implement effective regulation.

(b) The CCCFA is intended to protect a particular class of consumer borrowers. Whereas the Credit Contracts Act 1981 applied to all credit contracts, the CCCFA applies only to consumer credit contracts.[36] The regulation implemented by the CCCFA applies only

[36] Credit Contracts Act 1981, s 3(1)(a).

in that market. The failure of the prior legislative scheme was a primary driver for the CCCFA's enactment.

(c) The legislature decided, as a matter of policy, to regulate fees by focussing on cost recovery. The process established in ss 42 and 44 is one of building up to the costs required to carry out an activity. The implications of listing the relevant activities in s 42, for example, is to make clear that the costs of other activities are not relevant under that provision, and cannot be classified as establishment fees. Costs that cannot be correctly brought within any of the statutory definitions of fees are available to be recovered as interest. So, the CCCFA proscribes recovering all costs, leaving some to fall within the ambit of interest recovery. This is reflected in the structure of the "light-handed" provisions governing interest.

(d) The structure and content of s 43 supports this interpretation of the other sections dealing with fees. Section 43 governs prepayment fees. It is prescriptive, ensuring that fees match costs and requires costs recovered to be related to the particular transaction in question. Section 43 is a closed provision; it sets out in advance the fees that can be charged on the occasion of prepayment and the level of fees is clearly limited to the reasonable estimate of loss occurring upon prepayment. The operation of that section reflects the way the Commission's interpretation of ss 41–44 would operate.

(e) The starting point for interpreting and identifying the definition of reasonableness is in: (i) the various definitions in s 5, (ii) ss 42 and 44 (both of which are prescriptive) and (iii) s 41 in which unreasonableness operates as a general guiding principle. At the final stage of analysis, s 41 still leaves the option open to the creditor to put into issue some other factor which might be relevant to what is a reasonable fee. But any factors of this kind must still be relevant to and consistent with the context and text of ss 42 and 44. For that

reason, "reasonable standards of commercial practice", which is listed only in s 44, cannot be drawn into a s 42 inquiry.

(f) The wording of s 41, granting the court power to order relief "if [it] is satisfied" a fee is unreasonable leaves open the burden of proving reasonableness, as the circumstances change. Although in most cases it is for the Commission, when alleging a creditor has charged unreasonable fees to discharge this burden, it is also consistent with that provision for the court to require proof from the creditor as to the basis of its fees, to satisfy the court as to their reasonableness.

(g) Costs must be identifiably connected to the activity in question. There is no basis on which to utilise a "subjective test" of beneficial relationship, being determined by the creditor itself. Rather, costs incurred rest on a spectrum. At one end, direct variable costs, which are paid only when the loan contract is entered into, have a clear causative relationship with the fee-related activity. At the other end of spectrum, some indirect, fixed costs are excluded from recovery. The costs that lie in between must be proved by the creditor to be referable to a relevant activity, generating fees – they must be proved to be reasonable. The further away from a variable cost the expenditure lies, the harder it will be to link to loan transaction (or to activities related to the loan transaction). The Commission submits the line between reasonable and unreasonable fees should be drawn closer to the variable costs, with a link to the loan transaction clearly identifiable, in light of the CCCFA's mandate for consumer protection.

[50] Finally, Mr Mills referred to the process map prepared by Mr Cregten, explaining how MTF went about allocating costs to fee activities, which Mr Todd (MTF's Chief Financial Officer) accepted as accurate at a general level. Mr Mills contended MTF's charges reflect the difficulties and complexities in applying a beneficial relationship test, seeking to recover all costs. Mr Cregten's assessment of the recoverable costs adopted on the basis of the Commission's test were also

broadly accepted as accurate by both parties, if the Commission's approach were to be favoured. At root, therefore, the experts were divided only by the correct test to be applied to the "reasonableness" determination.[37]

Our decision

Analysis

[51] We consider the Commission's approach is correct. The purpose of the fee provisions in subpart 6 of the CCCFA is clearly to restrict the costs that can be recovered as fees. As the heading to the subpart makes clear, the aim is to identify and proscribe "unreasonable fees". The principles set out in ss 42 and 44 create a scheme requiring the costs a creditor seeks to recover in respect of a particular fee activity to be "sufficiently close and relevant" to that activity.[38]

[52] We accept the Commission's approach for the following reasons. First, the required connection in the provisions between the relevant fee and the costs incurred in generating it supports this approach to fees. Fees must recover costs only generated "in connection with" (in s 42) or "in relation to" (in s 44) the activity to which fees are said to relate. In *Hatfield v Health Insurance Commissioner* the Federal Court of Australia held, in respect of similar wording, the nature of the required connection, be it close or of wider ambit, will turn on the object and purposes of the particular statutory provision.[39] An example of the need for a close connection arose in this Court in *Strachan v Marriott* where the issue was whether potential tortious liability of the directors of a solicitors' nominee company fell within the phrase "all costs, fees and expenses in connection with the formation, registration … management, operation and winding up" of the company.[40] This Court acknowledged the words could be interpreted broadly, but held instead by majority that the words should be given a more restrictive interpretation, consistent with the statutory objectives.[41]

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37 We note that on appeal, the appellants now allege some inconsistencies in Mr Cregten's calculations, adopted by the High Court. We will address this later, when we assess relief.

38 Quantum judgment, above n 2, at [66].

39 *Hatfield v Health Insurance Commission* (1987) 15 FCR 487 at 491 per Davies J.

40 *Strachan v Marriott* [1995] 3 NZLR 272 (CA) at 279 per Hardie Boys J.

41 Compare the similar analysis of Savage J in *Yurjevich v Commissioner of Inland Revenue* (1991) 13 NZTC 8,185 (HC) at 8,189.

[53] In *IAG NZ Limited v Jackson* this Court applied *Hatfield* with approval.[42] That case concerned an insurer attempting to establish a nexus or relationship between dishonest conduct and civil liability, to exclude cover for liability incurred when delivering professional services. The need for a causal relationship between the two concepts was required by the exclusion clause in the insurance contract for civil liability, "in connection with" dishonest acts or omissions.[43]

[54] We have considered the legislative history in relation to the text of ss 42 and 44. We agree with Mr Mills' observation that the CCCFA was intended to protect a particular class of vulnerable consumers by ensuring transparency and disclosure in credit contracts. Borrowers who may be less financially literate were a particular concern. Thus to advance this object of transparency and disclosure, Parliament sought to limit establishment fees to a level reflecting the actual and identifiable costs incurred by the creditor making the loan. At the same time, Parliament chose not to regulate interest rates. Interest charged by a creditor was subject only to a test of oppression.[44] We consider this statutory context supports a narrower interpretation of these provisions than that advanced by the appellants.

[55] It is also relevant the CCCFA allowed lenders to impose any type of fee provided that it was not unreasonable. As the explanatory note to its Bill form describes, "unreasonableness in respect of establishment and prepayment fees is defined and a general standard is set for other fees".[45] The explanatory note also observed, in relation to s 42 (cl 37), the "test is designed to ensure that creditors match fees to the specific cost of the matter giving rise to the fee" and further, in relation to s 44 (cl 39), the test is "designed to encourage creditors to match fees to the specific costs of the matters giving rise to the fee".[46] We consider this supports the interpretation of reasonableness and "in connection with", "in relation to" requiring costs recovered through fees to be closely connected to the matter giving rise to that fee.

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42 *IAG NZ Ltd v Jackson* [2013] NZCA 302, (2013) 17 ANZ Insurances Cases ¶61-982.
43 At [29]–[30].
44 CCCFA, pt 2, subpart 5, ss 36–40.
45 Consumer Credit Bill 2002 (2–1) (explanatory note) at 8.
46 At 8.

[56] Recent amendments to the CCCFA in 2013 posited the potential removal of the phrase "reasonable standards of commercial practice" from s 44. In retaining the phrase, the Select Committee emphasised:[47]

> [T]he reasonable standard consideration should be subordinate to the principle that credit fees and default fees should only reasonably compensate the creditor. Our amendment confirms and makes it clear that reasonable standards of commercial practice are not intended as a separate basis for calculating credit or default fees, but only to inform the main test (which concerns costs and losses).

[57] We accept Mr Goddard's point that once the comparison between the fee charged for the particular portion of the lending services has been compared with the costs of providing that service, as mandated by s 42, it is open to the creditor to put in issue some particular factor which might impact, in the specific circumstances of that case, on what is reasonable. This opportunity arises as part of the prescription in s 41 that a consumer credit contract must not provide for a credit fee or default fee that is unreasonable.

[58] However, we consider there is little scope for holding reasonable under s 41 an establishment fee that exceeds the creditor's average reasonable costs in relation to the four matters identified in s 42(a). Section 41 is silent on the question of onus of proof it requires. Section 41(2) provides that if the court is satisfied, on the application of the Commission or other party such as a debtor, that a credit or default fee is unreasonable, it may make certain orders. Plainly there would be an evidentiary onus on the party making the application. However once that onus is discharged, any proof of the existence of a factor particular to the case in point, other than the costs referred to in s 42, would need to be established with the evidential onus resting on the creditor. MTF was unable to point to any particular factor to demonstrate the additional fees it charged in respect of costs not closely connected to the establishment fee activities were reasonable.

[59] We also consider the specific wording of each provision in question supports our conclusion. The statutory definition of establishment fees refers to fees or charges that relate to the costs of four particular aspects of the credit contract

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[47] Credit Contracts and Financial Services Law Reform Bill 2013 (104-2) (select committee report) at 9 (discussing cls 24–26).

transaction.[48] The relevant costs to be recovered are those relating to the four activities listed in that definition.[49] This definition expressly excludes any fee or charge for an "optional service". In excluding those services, then, it is apparent the definition focuses on costs involved in all steps by which the creditor first provides credit to a debtor. This is significant in identifying what aspects of the credit transaction the legislature was seeking to capture in this section – namely controlling only those costs closely related to that part of the financial service.

[60] Analysing s 44, the use of the definite article before "matter", "creditor" and "debtor" introduces a specific focus on the creditor's reasonable costs and the creditor's reasonable estimate of any potential loss, relating to credit and default fees. We agree with Mr Mills that by clear implication, other costs are not relevant outside these two categories. While the structure of ss 44 is different to s 42, the statutory emphasis is still on actual, specific costs and the specific quantum of estimated loss.[50]

[61] The identification of specific costs and their control with reference to unreasonableness is no accident. We consider it was the clear intention of the legislature to define unreasonable costs by identifying specific activities and costs, and requiring a link to them, and through that link fulfilling the requirement of "reasonableness". This is apparent from the repetition of the phrases "in connection with" and "in relation to" specific activities or specific classes of activities, after the words "the creditor's reasonable costs" in the provisions forming part of the fee scheme.

[62] In light of our findings, we consider the application of each relevant provision at issue before us calls for a three-stage analysis. Section 42 requires:

(a) First, any fees charged under this section must comply with the definition in s 5; the fees must be connected to and have close

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48 Above at [29].

49 Being the application for credit, processing and considering that application, documenting the contract, and advancing the credit.

50 We agree with Asher J in *Commerce Commission v Avanti Finance Ltd* (2009) 9 NZBLC 102,662 (HC) at [31] (a case concerning s 43) that the phrase "reasonable estimate of loss" involves an estimate of an amount that will do "no more than compensate the creditor for the actual losses it could expect to sustain in the event of prepayment".

relevance to costs incurred by the creditor in the listed activities falling within the ambit of "establishment fee" activities. What is required is proof of a relevant sufficiently close relationship between the fee and the costs incurred in connection with the four discrete activities.

(b) Second, the Court is to inquire as to whether the amount of the fee in question is "equal to or less than" the creditor's reasonable costs in connection with those four activities. The focus is only the reasonableness of the costs incurred in connection with the four specific activities in s 5. There is no requirement nor any analytical need for comparison of fees within the market, or any "benchmarking" exercise. These first two steps serve to emphasise and demand an inquiry deliberately limited to the enumerated factors, prescribed by Parliament.

(c) Third, s 41(1) provides for a limited scope to introduce additional grounds for inquiring whether the credit contract provides for an unreasonable credit fee. Given the prescribed nature of the inquiry to this point, any such additional factors ought to be compelling and clearly relevant to and consistent with the statutory purpose noted earlier in this decision. Nonetheless, this statutory structure once again emphasises that actual costs are the decisive criterion.

[63] Accordingly, we agree with the Judge that there must be a close connection between the fee charged and the costs incurred in generating that portion of the credit service. We do not consider it is helpful to import any reference to the objective bystander. That is not the statutory test and we consider its use would also detract from the key focus on costs.

[64] Turning now to s 44, and applying the same interpretive standard set out above to its terms, we consider the inquiry will proceed in respect of credit and default fees in a broadly similar way to s 42. However, given the absence of

specific, defined activities in relation to which costs may be recovered, the analysis may be slightly different.

[65] First, therefore, the definition in s 5 will guide the assessment of what particular category of fee is being charged. Section 44 reflects the absence of discrete fee activities in the definition of credit and default fees, excluding certain types of fees from its application to enhance clarity.

[66] Second, the fee must be assessed in relation to whether it reasonably compensates the creditor for any cost incurred by the creditor in providing the fee-related service, or any loss incurred by the creditor in relation to the debtor's actions. Given the lack of specificity found in s 42, this structure makes sense. Section 44 requires the fee being charged to relate to the service generating the cost it recovers – as opposed to listing specific activities constituting "credit" or "default" activities. This requires a slightly closer analysis to assess the service it relates to and whether that is a credit or default fee-related activity and a careful application of the close connection test. It also makes sense, here, to include reasonable standards of commercial practice as a further element in the assessment, when lacking actual prescribed activities against which to assess costs and fees.

[67] Third, the same considerations for s 41 apply here, as with s 42.

Practical issues

[68] When it comes to practical application of the statutory language in ss 42 and 44, the need for a close, relevant connection provides a workable standard. The statutory obligations in both ss 42 and 44 to have regard to costs of specific activities of the creditor do not sit comfortably with the argument of Sportzone/MTF that the statutory language permits the inclusion of all reasonable costs of offering a finance facility. If the CCCFA permitted the recovery through fees of a portion of all costs of the finance business, it would dilute the regulation of fees to such an extent that it offers virtually no regulation at all. It would be tantamount to using a broad, oppressiveness standard, where the only clear regulatory guidance is the "benchmark" of fees charged by competitors. This approach is inconsistent with the

statutory purposes of transparency and consumer protection. It is also contrary to the wording of the provisions and definitions themselves.

[69] The Judge held a variable cost would always meet the "close relevance" test, although the actual amount of the cost would still need to be reasonable.[51] Mr Smith's evidence (referred to earlier at [42]) supports the proposition that it is a relatively simple process to identify costs that can be readily attributable to particular fee-related activities, particularly if they are variable costs.

[70] In terms of practicality, both parties called expert evidence. Such evidence is of course strictly irrelevant to our statutory analysis. However the parties and others with an interest in these issues may be assisted by an expression of our views on the proper accounting approach flowing from our interpretation of the statutory provisions.

[71] We agree with the Commission's approach that the principles of management or cost accounting are of assistance in providing practical guidance for the assessment of the reasonableness of a fee. The Commission's expert witness, Professor Bowman, supported the adoption of an appropriate accounting approach in determining the reasonableness of fees charged, by assessing the particular fee against the variable costs of the activity giving rise to the fee. Professor Bowman drew a distinction, for example, in respect of an establishment fee, between assessing the fee against variable costs incurred in establishing a consumer credit contract as opposed to the fixed costs that are incurred irrespective of the number of contracts entered into (and therefore fee-related activities). His analysis was based on the premise that fixed costs should not be recoverable.

[72] Applying a cost accounting methodology (an approach developed for the internal allocation of costs within a firm between different activities) allows a creditor to accurately allocate both fixed and variable costs, and direct and indirect costs, to activities to which they are closely connected. When applied to credit contracts, each type of costs must be related to the service provided. This was

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[51] Liability judgment, above n 2, at [83].

described in the evidence as the "cost object". Professor Bowman distinguished between these concepts, conveniently summarised by the Judge as:[52]

> (a) Direct costs are costs that are easily identified as relating to a cost object within an organisation.
>
> (b) Indirect costs are costs that relate to a productive activity of a company but cannot be readily identified with a particular cost object.
>
> (c) Fixed costs are costs that are independent of the volume of a cost object (the output).
>
> (d) Variable costs are costs that change in proportion to the volume of a cost object.

[73] These terms apply to a wide range of tasks undertaken by Sportzone/MTF.

[74] Professor Bowman concluded the approach of MTF in allocating virtually all of its company overheads (being fixed and often indirect costs) to fees was not a reasonable accounting practice. MTF's attempt to justify its fees by reference to costs that are fixed and not affected by its output of consumer lending (such as overhead costs unconnected with the activities giving rise to each fee) was therefore inappropriate.

[75] Professor Bowman considered that the statutory language of ss 41–44 supported the use of only variable costs, whether direct or indirect, being recoverable through the relevant fees. From an accounting perspective the statutory focus on particular activities within the credit transaction did not support the recovery of fixed costs through fees. Toogood J adopted this approach, tempering it with the framework advanced by Mr Cregten, who conceded some fixed costs may properly be recoverable by fees, when proved to be closely connected and allocated accurately.[53]

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52 Liability judgment, above n 2, at [73].
53 Liability judgment, above n 2, at [84].

[76] We agree with Toogood J's approach. We also agree the "beneficial relationship" test suggested by Professor David Lont for Sportzone/MTF is inappropriate. It is significant that Professor Lont himself acknowledged this test becomes subjective once it moves beyond cause and effect, and is more difficult to relate to the statutory requirements. Toogood J rejected this test, stating:

> [82] That approach cannot be justified by what I have determined to be the proper inquiry. Despite Professor Lont's careful and comprehensive analysis and discussion of the accounting principles, and Mr Kensington's support for it, I am unable to accept the fundamental proposition that the CCCFA permits the defendants to recover through fees all costs which can be demonstrated to have some beneficial relationship with the matter or activity in question, no matter how tenuous. Taken to its logical conclusion, the full cost absorption approach redefines the concept of reasonableness in terms of merely identifying a beneficial connection between the cost and the cost object and ensuring that a rational allocation of overheads between cost objects is made. While that approach may be open on the meaning of the expressions "in connection with" and "related to" taken in isolation from text and purpose, the reasonableness standard under the CCCFA is not to be determined from the point of view of a reasonable accountant advising management as to the appropriate allocations of costs for management purposes. To the extent that an accounting method provides a tool for meeting the purposes of the CCCFA, it must assist the application of the close relevance test … which I consider to be required by the statutory wording considered in the context of the statutory purposes.

[77] We consider the Judge was correct to do so. Professor Bowman agreed with Professor Lont that a successful company must recover all of its costs, both fixed and variable. Moreover, prices must be set at a level that will recover these costs. Companies in the business of providing consumer credit to borrowers, however, generate their revenue by lending at an interest rate higher than they pay for their funds. Their business is not the charging of fees alone. While some costs can and should properly be recovered through fees, the primary source of cost recovery is through net interest; being the margin between interests on funds lent and the cost of acquiring those funds. Accordingly Professor Lont's comments did not assist with determining how to assess the reasonable costs of MTF and Sportzone in connection with (or in relation to) several very specific activities, prescribed by law.

[78] Professor Bowman's evidence was supported by Mr Cregten. He considered the application of the statutory provisions to the various fees in question involved no single right or wrong method of allocating costs or management accounting purposes. The CCCFA sets out what creditors may and may not recover by way of

fees with reference to costs. As such, the cost allocation model is designed to identify and measure those costs for the purpose of that exercise, which is much more prescriptive and objective – precisely to ensure workability for commercial performance purposes.

[79] Mr Cregten proposed an approach involving examining the underlying activities and associated costs attaching to those activities, rather than adopting a more general cost apportionment approach. The most appropriate way of doing this is to utilise a variation of the "variable costing" approach, as he proposed. This identifies the costs that specifically relate to the activity that generates fees. Some direct variable costs will apply and others will be indirect. There may be some fixed costs, as Mr Cregten identified, that can be proved to be relevant and closely connected to fee activities. There will also be a residual category of costs or business overheads that have no relationship to the relevant activity.

[80] Both Professor Bowman and Mr Cregten were satisfied the accounting information they had reviewed strongly suggested that both MTF and Sportzone had adopted an inappropriate approach to determining their reasonable costs for the object of calculating fees. It would result in the recovery of costs through fees unrelated to the activity. We consider that the approach of Professor Bowman, supported and varied by Mr Cregten, best achieves the statutory purposes of transparency and consumer protection with regard to fees charged by creditors.

[81] For the above reasons we uphold the judgment of Toogood J on the first and second issues. It follows the Judge was correct in the liability judgment to hold the fees of Sportzone/MTF were unreasonable under s 41 of the CCCFA.

Is relief available under s 94?

[82] When the High Court considered the question of quantum, the Commission sought orders under s 94(1)(b) of the CCCFA for the repayment of amounts by MTF, reflecting the unreasonable portion of the fees on behalf of the relevant borrowers under the 39 credit contracts.[54] At the conclusion of the quantum judgment,

[54] Quantum judgment, above n 2, at [14]–[15].

Toogood J reserved leave to apply for formal orders under s 94(1)(b) directing the payment of refunds to the borrowers named in the proceeding. Sportzone/MTF challenge the Commission's right to seek such orders under s 94 on the basis that this Court has no jurisdiction to make the orders and the Commission has failed to prove loss.

[83] This question of jurisdiction requires consideration of the Court's general power to make orders under pt 4, subpart 3 of the CCCFA. This power to make orders is contained in s 93, which relevantly provides:

> The court may make all or any of the orders referred to in section 94 if the court finds that a person (whether or not that person is a party to any proceedings) has suffered loss or damage by conduct of any creditor, lessor, transferee, buy-back promoter, paid adviser, or broker that constitutes, or would constitute,—
>
> (a) a breach of any of the provisions of sections 17 to 82:
>
> (b) aiding, abetting, counselling, or procuring any other person to breach any of those provisions:
>
> …

Submissions of the parties

[84] Mr Goddard submitted the scheme of the CCCFA was that where a consumer credit contract provided for fees that were unreasonable, the remedy available to the Commission (or others) was to seek orders under s 41(2) that the fee be annulled or reduced.[55] Any proceeding of that kind must be filed within the one year limitation period in s 41(4). Section 41 thereby establishes a stand-alone remedial regime. Here no claim was brought within the limitation period. It is therefore too late.

[85] Before us, although not in the High Court, the argument was developed to contend that s 93 (and hence s 94) did not apply to s 41 because the proof that a fee is unreasonable is not such as to constitute a breach of that provision. Mr Goddard submitted s 41 was framed in a manner that focuses on the existence of a state of unreasonableness in respect of the fee concerned: the provision looks at what may be provided in a consumer credit contract. The section does not proscribe or prohibit

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[55] These orders may also be sought by a debtor or guarantor.

conduct on the part of a named actor.[56] Nor does it require or oblige conduct on the part of a named actor.[57] Thus no person can be said to have breached that provision. Thus where the CCCFA intends either to impose a requirement on a creditor, or to regulate what is contained in a credit contract, it expressly makes provision for each of those matters by referring to an actor and to the required/prohibited conduct directly.

[86] Mr Mills argued there is nothing in the CCCFA that supports that approach. Section 41 requires that a credit contract "must not" provide for a credit fee or default fee that is unreasonable, and not, as Mr Goddard put it, what may be provided. Mr Mills submitted that if a contract does provide for an unreasonable fee, this constitutes a breach of the prohibition in s 41.

[87] Mr Mills contended a consequence of the appellants' argument is that an unreasonable credit fee is not a breach of s 41, and accordingly no criminal proceeding could be brought as a result of unreasonable fees being charged. This is contrary to previous practice of the Commission and is also contrary to the approach in the High Court decision in *Commerce Commission v Bluestone Mortgages NZ Limited.*[58] Accordingly Mr Mills submitted that the primary remedies for s 41 are contained in ss 93 and 94.

Our analysis

[88] We reject the submissions for Sportzone/MTF. We do not consider the Court's power to be limited in such a manner. First, it is highly unlikely Parliament intended to limit remedies to annulment or reduction only, as provided for in s 41(2). Second, Mr Goddard cited no authority for the proposition that non-compliance with a provision worded like s 41 does not involve a breach of the statute. Moreover,

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[56] Compare for example CCCFA, s 38(1): "A creditor must not … require payment of or debit the interest charge".

[57] Compare for example CCCFA, ss 46 and 50: "A creditor must credit each payment made under a consumer credit contract to the debtor's account as soon as practicable after receipt of the payment" and "A creditor must accept any full prepayment … from a debtor at any time" respectively.

[58] *Commerce Commission v Bluestone Mortgages NZ Limited* [2012] NZHC 1946. Counsel referred to recent amendments to the CCCFA in which s 41(2)–(4) have been repealed. Equivalent provisions to those have now been inserted into s 94 as the new s 94(1)(ca): see Credit Contracts and Consumer Finance Amendment Act 2014, ss 29 and 60. These are triggered under s 94 by "a breach of any of the provisions of" ss 17–82.

there is no reason in principle why a prohibition such as s 41 must be directed to a named actor in order to qualify for the description of breach. Third, it is plain from the statutory context that the obligations in s 41 are directed to creditors or other persons imposing fees in consumer credit contracts.

[89] Therefore, the Court's power to make orders in the context of enforcement and remedies arises under s 93. The general power is triggered where the Court finds:[59]

(i) a person has suffered loss or damage;[60]

(ii) by conduct;

(iii) of an identified type of person such as a creditor;[61]

(iv) that constitutes, or would constitute, breach.

The word "that" in the fourth element is clearly a reference back to "conduct" in the second element. Mr Goddard's submission was that whoever the identified actor is from the list available in the third element must also be identified in the relevant provision (here s 41) for there to be jurisdiction under s 93. We see no reason to read the statute in that way.[62]

[90] The better reading is that the Court will have general power to make enforcement orders where a person suffers loss or damage; through conduct that constitutes a breach of any of the provisions in ss 17 to 82; and the person responsible for that conduct is one of the people named in s 93, that is, an identified type of person mentioned in element three above.

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59 As set out in CCCFA, s 93.

60 There is no necessity for that person to be party to proceedings: s 93.

61 Section 93 lists conduct by others including any lessor, transferee, buy back promoter, paid adviser, or broker: see above at [83].

62 The link between the conduct and the person who engaged in the conduct is made clear by the wording of s 94(1): "The types of orders that the Court may make against the person who engaged in the conduct referred to in s 93 are …".

[91] It is also instructive that, while s 93 refers to breach "of any of the provisions of ss 17–82", the structure of s 103, which creates offences occasioned by the breaching of the listed provisions, is different. It does not refer generally to ss 17–82 but rather refers specifically to certain identified sections; the offence section is applicable only to ss 17–74, 76–82, 83E, 83F, 83G, 83O, 83P, 83S, 83T and 83ZN.[63] Section 103 has specifically separated s 75, for example, into its own offence.[64] This suggests, if Parliament meant to likewise omit certain sections (such as s 41) from the scope of s 93 and create a parallel regime, it would have done so.

[92] Finally, given the limited scope of the remedy in s 41 (restricted to annulment or reduction of the fee) it is logical for Parliament to provide jurisdiction for additional remedies, upon proof of loss. We have no doubt that s 41 was not intended to cover the entire field of available remedies. The jurisdiction-grounding provision in s 93 should be given meaning to permit borrowers affected by unreasonable fees to obtain relief through the available remedies in s 94. That s 41 is not exclusive as to remedies is also supported with reference to s 48.[65]

[93] We therefore uphold the approach of Toogood J that there is power to grant orders, as found in the quantum judgment. The third issue is therefore answered in the affirmative. Relief is not restricted to remedies available under s 41.

Has the Commission proved any loss?

[94] Sportzone/MTF argue that, if there is power to make orders under s 94, the Commission has not shown that any of the 39 borrowers suffered loss or damage in this case. Mr Goddard acknowledged it is common ground that the appellants could have recovered through interest charges the costs that the Court found should not have been recovered through fees. He added that, if MTF had charged lower fees, the interest rate on those loans would have increased. He submitted there is no

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63 Section 103(1). This section is not yet in force but will come into force on 6 June 2015 or earlier by Order in Council: s 68 Credit Contracts and Consumer Finance Amendment Act 2014.

64 Section 103(2).

65 Section 48 covers the situation where a debtor makes a payment to a creditor that the creditor is not entitled to receive. If so, the creditor must refund or credit the payment to the debtor as soon as practicable under s 48(1). This applies despite any agreement to the contrary (s 48(2)).

evidence that the net result would have been favourable to any of the borrowers to whom the pleadings relate.

[95] We are not satisfied the position is as the appellants postulate. To the extent the appellants wished to advance it at trial, they had an evidential onus to do so. Proof of loss for the purposes of s 94 was not a central focus of the High Court evidence or argument. Mr Mills accepted that the argument had been first emphasised in closing at trial. But he submitted that it was not addressed in any detail in the evidence. Nor, he argued, was it raised with any particularity in the appellants' pleadings. The statement of defence was simply a bare denial that the borrowers had suffered loss. Accordingly the Commission's pleaded position during the evidence at trial was that on the facts of this case, loss or damage was sufficiently established by the fact that the fees concerned had exceeded recoverable costs.

[96] Section 94 of the CCCFA lists the type of orders that the Court may make against the person who has engaged in the conduct referred to in s 94. It lists at subpara (b) a possible order:

> Directing the person to pay to any person who has suffered loss or damage by that conduct an amount not exceeding the amount of the loss or damage (to the extent that any statutory damages that are to be paid do not adequately compensate the person for the loss or damage):
>
> …

[97] Statutory damages are not relevant here, so the only question is whether any one of the 39 borrowers "has suffered loss or damage by [MTF's] conduct". We consider a borrower has plainly suffered loss or damage if he or she has paid an unreasonable fee. The loss is the amount by which the fee exceeds what the creditor is lawfully entitled to charge, the borrower would not have paid this excess if the fee was reasonable. The necessary causal connection is established.

[98] We are satisfied that Mr Goddard's argument as to what might have happened with regard to MTF increasing interest rates is speculative. There is no evidence that a particular borrower would have entered into a loan transaction with MTF at a higher interest rate if the establishment fees had in fact been reasonable. A borrower

may well have gone to another lender who, because of efficiencies in its business operation, was able to charge a lower interest rate.

[99] We are also concerned that if Sportzone/MTF had wished to focus specifically on an omission by the Commission to prove loss, the defence ought to have been the subject of a clearer and more detailed pleading and evidence in the High Court. The evidence in the High Court has been left in a wholly unsatisfactorily position. Sportzone/MTF ought not, on appeal, to be able to benefit from an argument of this nature on appeal.

[100] Sportzone/MTF fail with this ground of appeal.

Does s 45 assist MTF?

[101] On appeal, but again not in the High Court, MTF sought to rely on s 45 of the CCCFA to immunise from scrutiny by the court the fees charged by MTF to Sportzone.[66] Section 45 provides:

> **45 Fees or charges passed on by creditor**
>
> (1) A fee or charge payable by a debtor for an amount payable or to reimburse an amount paid by the creditor to another person, body, or agency must not exceed the actual amount payable by the creditor if that amount is ascertainable when the fee or charge is paid by the debtor.
>
> (2) The actual amount payable must be determined by taking into account any discount, rebate, or allowance received or receivable by the creditor or any related company.
>
> …

[102] The argument arises in the following context. The relevant credit contracts were entered into between Sportzone and the debtors. Sportzone borrowed a corresponding amount from MTF, paying certain fees to MTF that Sportzone then recovered from the debtors. Sportzone also charged its own fees. The fees Sportzone charged to the debtors were designed to recover fees payable by Sportzone to MTF including the MTF establishment fee and the MTF account

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[66] As a result of issues arising on this topic late in the appeal argument, counsel for the parties were given leave to file memoranda post hearing.

maintenance fee. In addition, Sportzone charged the debtor fees that it retained and did not pass onto MTF or other third party.

[103] There is no dispute the relevant credit contracts were assigned by Sportzone to MTF by way of security, immediately upon entry into the contract. MTF thereby became a creditor by the time of the assignment. MTF argues the assignment does not affect who their fees are payable by and to under the relevant contractual arrangements. Here the fees were payable by the debtor to Sportzone. Mr Goddard accepts that none of this is a matter of evidence. Rather it is apparent on the face of the relevant contracts. Mr Goddard also accepts that in the absence of an assignment of the contract by Sportzone to MTF, it would be clear that s 45 applies to the fees charged by Sportzone to a debtor to recover fees paid by Sportzone to MTF.

[104] The fact that the position now advanced by MTF is apparent on the face of the contracts is not a complete answer. Mr Mills, not unreasonably, submitted if MTF's new argument had been raised in the pleadings or at trial the Commission may have sought to amend its pleadings to say, even if MTF were not a "creditor" of the borrowers under the CCCFA, it may have been liable as an accessory to the breaches of Sportzone or was in substance a party to a consumer credit contract with borrowers because it was integrally involved in the entire transaction.[67] If proved, MTF's agreements with Sportzone could have been treated under s 7(2) as "a credit contract made at the time when the contract, or the last of those contracts, or the arrangement, was made …".

[105] Moreover, had the matter arisen at trial the Commission would have wished to cross-examine the appellants' factual witnesses on a range of significant evidential matters. There would have been a greater emphasis at trial, rather than examining the reasonableness of the fees charged by the appellants, on determining who ultimately paid the fees charged by MTF and the relevant accounting treatment of the fees and the circumstances in which Sportzone would be liable for fees for customers who did not take up the offer for finance or cancelled their agreements early. Further, issues of the practical extent to which MTF exercised its rights (or

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[67] CCCFA, subs 93(b)–(e) and s 7(2) respectively. This latter provision deals with a transaction that is "in substance or effect a credit contract".

those of Sportzone) directly against defaulting borrowers would have been examined.

[106] We are of the view that these concerns have real substance. Given however that the question of reliance on s 45 was not pleaded, was not the subject of evidence or submissions or a decision of the High Court, we conclude that it would be unfair and improper for the matter to be determined for the first time on appeal. It is too late for the appellants to raise such arguments.

[107] Assuming the issue were live, we see real difficulties in the arguments advanced. Sportzone/MTF agree with the Commission that in principle s 41 is also capable of applying to a fee charged by a creditor to recover a fee payable by the creditor to another person. Section 41 is expressed in general terms. While s 45 is intended to protect a creditor charging a debtor a fee that has been passed on from a third party source, it is plainly not intended as a blank cheque where the fees passed on are themselves unreasonable under s 41.

[108] We agree that the statutory language and context gives rise to an implication that s 45 is subject to s 41. In the normal course the basis for a fee of the type covered by s 45 being examined would arise if there is a link between the entities or where the pass-on company is under investigation. In such situation there is no reason why the law should not require the fees to be reasonable.

[109] Even on the evidence currently before the Court, we consider s 45 cannot avail MTF. MTF is a party to, and an integral part of, the consumer credit contracts between Sportzone and its customers. It was common ground that MTF was a "creditor" of those customers. It is therefore subject to the provisions of s 41 and subject to the remedial regime in ss 93–94.

[110] Those sections permit the Court to make orders against creditors as well as those who aid, abet, counsel or procure another person to breach the provisions of the CCCFA. It is common ground that the conditional purchase agreements in this case are consumer credit contracts.

[111] Section 5 defines a creditor as including anyone who provides credit under a credit contract, who *may* provide credit under a credit contract and includes the assignee for the time being entitled to the creditors rights. It follows that one or more persons may be a "creditor" under a consumer credit contract at any given time including a financier such as MTF.[68] The statement of defence of MTF and MTFS accepts that MTF is a "creditor" from the time of assignment of the credit contracts. Assignment is triggered by the execution of the conditional purchase agreements and occurs contemporaneously with the establishment of the credit consumer contracts.[69] Thus, MTF became a creditor from the moment of execution of the agreements and at the same time as Sportzone.

[112] Accordingly both Sportzone and MTF (through the agency of Sportzone) are parties to the consumer credit contracts at issue.[70] It is true that MTF is a party for limited purposes; but such purposes include taking the assignment of Sportzone's interest and stepping into the shoes of Sportzone in exercising its rights if required. Both MTF and MTFS are included within the definition of lender.[71] MTF's fees are separately specified and charged. Ultimately such fees are paid by the borrower to MTFS. Usually the dealer will neither pay nor receive the MTF fees.

[113] In these circumstances we are satisfied that, if we were required to decide the point, s 45 would not avail MTF. We accordingly reject this ground of appeal.

What is the quantum of loss?

[114] We have already referred to the quantum judgment of Toogood J that followed the liability judgment and a separate hearing to address the quantification of remedies under s 94(1)(b) of the CCCFA. The quantum judgment determined the Commission's claims for remedies in respect of some categories of costs about

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68 *Gault on Commercial Law* (online looseleaf ed, Thomson Reuters) at [4C.2.01(2)(a)].

69 Clause 1.0–2.0, Section 2 "Financial arrangements and transfers" of the Conditional Purchase Agreements (between Sportzone and borrowers).

70 There is a further factual question as to the definition of credit fees in s 5, being paid to "or for the benefit of" a creditor – its potential application, although not raised before us, and how it might interact with the provisions noted above is a further factor that may have become relevant had this been the subject of full argument.

71 Clause 12.1 (definition of "Lender") of Section 1 "Credit contract" of the Conditional Purchase Agreements (between Sportzone and borrowers). See also Clause 11.1 (applying "Lender" as defined term).

which the parties have been unable to reach agreement. The principles applied by the Judge in determining the remedy claims were those set out in the liability judgment.

[115] The quantum judgment addressed a number of particular costs relied upon by MTF to justify the establishment, account maintenance and arrears fees which it charged in the relevant years. The quantum judgment contained a detailed analysis of the various cost items claimed by MTF in the light of the evidence produced by the Commission.

[116] Toogood J made a number of detailed findings as to the correct allocation of costs to fees. We do not propose to revisit that detail here. We set out below some examples of the key findings to illustrate the practical approach the Judge undertook:

(a) Before turning to the extent to which the fees were unreasonable, Toogood J addressed the cost items relied upon by MTF, which he considered cannot be held to be connected with or related to any of the fees it charged. These included training costs (which inherently cannot be closely relevant to a particular transaction), travel costs (which MTF never attempted to explain with reference to a particular loan transaction or loan activity), directors' fees and travel costs (which were also not clearly linked to any specific loan transactions) and professional and accounting, legal and audit fees.[72]

(b) In respect of establishment fees, Toogood J assessed each of the "cost centres" to which MTF had allocated its fees. This was then broken down even further to the specific line items, the cost of which the fee was said to recover. For each of these, the Judge went through each of the heads of costs, determining whether it was closely relevant or not, and if so, what percentage recovery should be permitted under each fee category including:[73]

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[72] Quantum judgment, above n 2, [43]–[50].

[73] In respect of establishment fees: at [54]–[94]; in respect of account maintenance fees: [95]–[104] and in respect of arrears fees: at [105]–[116].

(i) 10 per cent of all staff salaries and performance schemes were attributable to activities covered by establishment fees;[74]

(ii) 10 percent of bank activity fees were allocated as costs recoverable by establishment fees;[75]

(iii) 10 per cent of banking, direct credit and debit facilities were allocated as costs recoverable by establishment fees;[76]

(iv) all treasury cost centre costs were disallowed, outside of the bank charges noted above;[77]

(v) hardware and software depreciation was allowed as recoverable indirect costs, allocated across multiple different fees on the basis of generally accepted accounting practice (as accepted by the Commission);[78] and

(vi) the Judge declined to allow any recovery for the cost of capital (being, as framed by MTF as the return on the capital as a fixed cost item), as it was not an actual cost incurred in the establishment of any loan.[79]

[117] The central attack by Sportzone/MTF on this part of the judgment under appeal is on the question of the statutory interpretation of the relevant provisions, rather than the details of the evidence and findings of Toogood J. We have upheld the approach of the Judge and we are satisfied it is correct.

[118] To the extent Mr Goddard challenges the detail of the assessments made in the quantum judgment, he contends the application of the principle by the Judge was inconsistent, pointing to a deeper problem with the test itself. This problem was

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74 At [56].
75 At [60].
76 At [66].
77 At [69].
78 At [86].
79 At [90]–[94].

illustrated by Toogood J's determination that certain elements of MTF's cost of capital were held to be too remote to be recovered through fees, while other costs of capital were held to be recoverable. An example is certain depreciation costs of hardware and software were held to be recoverable, whilst "other costs of ownership of the same facilities" were not recoverable, including treasury and securitisation costs. This was "inconsistent" and was said to belie a principled and conceptual error with this approach to determining fees generally.

[119] We are satisfied that the approach Toogood J adopted was applied correctly and we are satisfied the approach itself is sound and capable of precise and clear application. The issue above to which the appellants have referred does not convince us of an error on the part of the trial Judge or in the method itself. First, the quantum judgment itself explains the different treatment of these costs. Toogood J (and the Commission itself) accepted it had been proved that the cost of this depreciation was sufficiently connected to specific activities so as to be recoverable through fees relating to them. This is contrasted with his finding in respect of the cost of capital, which, as a number of steps removed from any loan transaction (constituting essentially return on capital investment by shareholders and the cost of doing business generally), the link to any fee-generating activity was simply too tenuous. That is a rational basis on which to differentiate between these costs and we consider that to be a correct application of the approach, rather than an inconsistent one.[80]

[120] One simple example will suffice to demonstrate the validity of the Judge's approach. The appellant originally claimed costs in respect of all of the time of the managing director (in 2006, allocated 97 per cent to establishment fees, 2 per cent to management fees, and 1 per cent to prepayment, in the following two years, 100 per cent allocated to establishment fees). This was relied upon in the evidence at trial and in the submissions prior to the quantum judgment. The trial Judge rejected the total cost claimed.[81] However during argument on appeal Mr Goddard accepted, when applying the methodology of Professor Bowman and Mr Cregten, the extent to

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[80] The appellants also contended, obliquely, that failing to allow recovery through fees of the cost of capital was inconsistent with the Commission's own Draft Guidelines, issued in March 2009. We do not consider this argument to be compelling – the guidelines in question are expressly stated to be subject to further judicial interpretation and guidance, have no legislative force, and are also in many respects consistent with the Commission's cost recovery approach.

[81] Quantum judgment, above n 2, at [46]–[47].

which the costs of the managing director could be claimed as relevant to any particular fee would turn on the facts of the case. He accepted that it was not appropriate, as MTF had done, to claim the whole of the time of the managing director.

[121] We are satisfied the Judge made no error applying the principles to the facts of the case. Accordingly the orders as to quantum apparent from the quantum judgment are upheld. This ground of appeal also fails.

Result and costs

[122] For the above reasons the appeal is dismissed.

[123] The Commission sought costs. Mr Goddard argued that this was a test case in that it raised a novel point of law with ramifications going beyond the particular case.[82] Sportzone/MTF submitted that the Commission itself recognised early in the proceedings that it wished to continue the claim against Sportzone despite it being put into liquidation, given the test nature of the case. Various authorities were cited in support of the contention that costs should, if the appellants were unsuccessful, lie where they fall. Counsel also referred to the express power of this Court in r 53F(e) to refuse or reduce an order for costs where an appeal concerned a matter of public interest and the party opposing costs acted reasonably in the conduct of the appeal.

[124] It is true that the appeal is the first of its nature to come to this Court. However we agree with the Commission's position that this is not a test case in the sense that it would justify a departure from the ordinary costs principles. Clearly it has not been pursued by MTF for the public interest or for non-pecuniary gain in the manner discussed by the Supreme Court in *Environmental Defence Society Inc v The NZ King Salmon Co Ltd*.[83]

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82 Andrew Beck and others (eds) *McGechan on Procedure* (online looseleaf ed, 2015) at [HRPt 14.17].

83 *Environmental Defence Society Inc v The New Zealand King Salmon Co Ltd* [2014] NZSC 167 at [12] per Elias CJ and William Young J, at [38]–[41] per McGrath, Glazebrook and Arnold JJ.

[125] Accordingly we are satisfied that costs should follow the event. The appellants must pay the respondent costs for a complex appeal on a band B basis and usual disbursements. We certify for second counsel.

Solicitors:
DLA Phillips Fox, Wellington for Appellants
Meredith Connell, Auckland for Respondent