

31 March 2015

Court of Appeal judgment released

The Court of Appeal hearing in the Sportzone case was held in November 2014 and a judgment has now been delivered. The Court of Appeal dismissed the appeal by Sportzone Motorcycles Ltd and MTF.

The Court of Appeal has upheld both the High Court's 'Liability Judgment', that some fees charged under the loan contracts were unreasonable in terms of the Credit Contracts and Consumer Finance Act 2003 (CCCFA), and the 'Quantification Judgment', which detailed specific costs that could be recovered by way of the relevant fee.

The High Court had rejected the Commission's claim that Sportzone and MTF failed to make proper disclosure of components of credit fees and that the labels used for establishment and account maintenance fees were misleading and deceptive in breach of the Fair Trading Act. Those aspects of the decision were not challenged by the Commerce Commission before the Court of Appeal. MTF has always fully disclosed the fees it charges and the level of those fees, so that all borrowers are fully informed.

The Quantification Judgment allows the recovery of many of the fixed and indirect costs the Commission originally sought to exclude as an unreasonable recovery through fees. In applying the Quantification Judgment there are increases of up to 1,500% from the single figure fees that formed the Commission's original position in the High Court. That original position was that each of MTF's establishment fees, for the 2006 – 2008 period, ought to have been less than \$10.

Consequently the amount by which the fees have been held to be unreasonable, and is to be repaid to 39 Sportzone borrowers, is less than \$10,000.

MTF is disappointed with the decision that the amount of some fees charged were considered unreasonable.

Both the Quantification Judgment and MTF fee models include a mix of interest rates and fees, as allowed for in the CCCFA. Both models include an analysis of recoverable costs.

MTF did not attempt to recover any costs other than the costs of running its finance business and did not make a profit from any of the fees charged. All costs recovered through fees were previously being recovered through the interest rate charged to borrowers. MTF specifically adjusted the average interest rate down by two percentage points to compensate borrowers for the introduction of the CCCFA fees model. The fee model meant that borrowers would pay interest for the use of money they borrowed, and fees for the costs connected to the services they received for the establishment and maintenance of loans, and the recovery of defaults. In MTF's view, the Court's finding does not acknowledge that without the fee model, borrowers would have paid higher interest rates on the loans to recover costs not recovered through fees and, as a result, had suffered no loss.

A key purpose of the CCCFA is to assist consumers to distinguish between competing credit arrangements. MTF's view is this judgment will not assist borrowers to identify any unreasonable fees charged by competing lenders. If two lenders charge exactly the same fee amount to establish a loan on the same terms, one of those fees may be unreasonable and the other not. The Court's view is that the determination is to be made almost solely by a complex cost accounting analysis that depends on the structure of each lender. It is highly unlikely that any borrower would be able to make such an assessment prior to taking out a loan. A borrower would not know whether a fee is unreasonable by simply looking at the dollar amount or any

benchmark against commercial practice. The fees charged by MTF and Sportzone are similar to those charged by many finance companies and banks in the New Zealand market.

The judgments relate to 39 loans, written in the 2006 – 2008 period in the absence, at the time, of any meaningful guidance from the regulator or Courts on the interpretation of new and non-prescriptive consumer legislation. The nature and structure of MTF's business has changed substantially since that time, as has its calculation of costs and fee setting process.

While not in a position to finally quantify any potential implications at this stage, MTF is well advanced in this process and hopes to work with the Commission to ensure the current fee model is compliant.

This case is significant and has implications for the consumer lending industry generally, as the principles will be incorporated in the Responsible Lending Code, which will take effect from 6 June 2015. The Code sets out the processes, practices and procedures that a lender should follow to ensure that fees are not unreasonable and will apply to all consumer credit contracts written after 6 June 2015.

MTF is currently considering whether to take any further steps in the proceedings.

As the matter remains before the Courts, MTF will not be making any further comment.

Background

On 27 January 2010, Motor Trade Finances Limited (MTF) advised that it had received notice of a High Court civil proceeding brought by the Commerce Commission against a shareholder in MTF, Sportzone Motorcycles Limited (Sportzone, (now in liquidation)), MTF and MTF Securities Limited. The Commission alleged breaches of the Credit Contracts & Consumer Finance Act 2003 (CCCFA) and the Fair Trading Act 1986 (FTA) in respect of various fees charged in 39 loan contracts originated by Sportzone between May 2005 and July 2008.

The High Court rejected the Commission's claim that Sportzone and MTF failed to make proper disclosure of components of credit fees payable under the loan contracts. The Court also rejected the Commission's claim that the labels Sportzone and MTF used for establishment and account maintenance fees were misleading and deceptive in breach of the FTA. The Commission subsequently abandoned its appeal on the FTA aspect of the case. Consequently neither matter was heard by the Court of Appeal.

Glen Todd
Chief Executive Officer

