FINANCIAL SERVICES FEDERATION

25 February 2019

Competition and Consumer Policy
Ministry of Business, Innovation & Employment
P O Box 1473
WELLINGTON 6140 By email to: competition.policy@mbie.govt.nz

Thank you for the opportunity for the Financial Services Federation ("FSF") to submit on the Discussion Paper: Protecting businesses and consumers from unfair commercial practices.

By way of background, the FSF is the industry body representing the responsible and ethical finance and leasing providers of New Zealand. We have nearly sixty members and associates providing financing, leasing, and credit-related insurance products to more than 2 million New Zealanders. Our affiliate members include internationally recognised legal and consulting partners. A list of our members is attached as Appendix A.

FSF members are therefore involved in providing products and services to both businesses and consumers as well as being recipients of products and services from other businesses. As such they can be both contractor and contractee.

As credit contract providers, FSF members are very familiar with the need to read and fully understand the terms of contracts before signing them. The following answers to the questions raised in the Discussion Paper therefore relate more to FSF members' experiences as the contract provider rather than from the point of view of them entering into a contract.

Before answering the questions raised in the Discussion Paper, the FSF points out that the financial services sector is heavily regulated in New Zealand in terms of the way in which it transacts with both consumers and businesses. At a broad level, therefore, the FSF supports the intention of the Discussion Paper to apply some of the same prescription for the way in which financial services businesses must operate to business more generally. The FSF does however have some concerns that in doing so, this could have the effect of placing more prescriptive compliance obligations and costs on to the financial services sector which is something the FSF believes should be avoided as much as possible.

1. **What types of unfair business-to-business contract terms are you aware of, if any? How common are these?**

FSF members do not report any situations where they have been subject to unfair business-to-business contract terms when they have entered into a contract to be supplied goods or services from a business contract provider.

FSF members do however report that it is their experience that when they are the contract provider, they will ensure that their contracts are fully disclosed to their customers, be they consumers or businesses. FSF members also take their responsibilities to ensure their contracts do not contain any unfair terms incurring significant legal costs to do so. FSF members report however that in spite of such scrutiny of their contract terms and full disclosure to customers, they have experienced customers – both consumer and business – accusing them of imposing unfair contract terms during the course of the contract.

An example of this would be where the contract allows for recovery of reasonable loss to the credit contract provider in the event of early repayment of a fixed interest rate loan. This is a provision that is perfectly legal provided that the credit contract provider recovers their reasonable loss and does not impose a further penalty on the borrower. Whilst this provision might have been considered fair by the customer at the time of entering into the contract, it might be construed by them as being unfair if it is invoked and they are asked to compensate the credit contract provider for their loss in the event of early repayment of the loan.

Another example cited by FSF members as being not uncommon is where their contract to provide a motor vehicle under lease provides that at the expiry of that lease, the vehicle is returned to them in reasonable condition – allowing for normal wear and tear. This provision can be construed by the lessee as being unfair if, in the view of the leasing contract provider, the vehicle has been returned in poor condition.

The FSF therefore submits that what might be construed as being "unfair" may very well not be and that the view as to what is or is not "unfair" can be very subjective.

**2. What impact, if any, do these unfair contract terms have?**

The FSF submits that ensuring that their credit contracts do not contain unfair terms adds considerable cost, particularly in legal fees, to the preparation of their contracts and this is part of the cost to them of doing business.

**3. Is government intervention to address unfair business-to-business contract terms justified? Why/why not?**

The FSF believes that for credit contract providers there is already sufficient legislation in place to prevent unfair contract terms in the business-to-business context. In particular, the Credit Contracts and Consumer Finance Act 2003 ("CCCFA") already makes it illegal for credit contract

providers to act oppressively in relation to their contracts with customers – be they consumer or business customers. The term "oppressive" is defined in section 118 of the CCCFA to mean "oppressive, harsh, unjustly burdensome, unconscionable, or in breach of reasonable standards of commercial practice". Further, section 124 of the CCCFA sets out the matters that a court must have regard to in deciding whether to re-open a credit contract under the oppressive provisions.

Due to the oppressive provisions in the CCCFA, the FSF does not believe that any further legislation would be required for credit contract providers to address unfair business-to-business contract terms – as a level of protection against such unfair contract terms already exists. However, the FSF would not object to all other industries and sectors being subject to similar such preventions against oppressive conduct if the Government felt that unfair business-to-business contract terms is a sufficiently large problem to require addressing.

If the Government were to introduce a lower threshold to deal with unfair business-to-business contract terms (i.e. something less than "oppressive"), FSF believes any such threshold would need to be clearly defined to provide affected businesses with sufficient certainty.

The FSF believes that what are "business-to-business" contracts would have to be clearly defined if the Government were to intervene to address unfair contract terms. What is deemed to be a "business" should also, in the FSF's view, be defined consistently across all legislation. It is also submitted that not all businesses would necessarily need the protection from any such new laws and, therefore, may be very large sophisticated businesses should be excluded from any protections.

In this regard, the FSF notes that the Financial Markets Conduct Act 2013 ("FMCA") draws a distinction between "retail" or "wholesale" customers and requires financial markets participants to apply higher standards of disclosure to retail customers than they would to those who are deemed to be wholesale. Maybe this type of distinction could be used as a basis to set what types of business-to-business contracts should be subject to any new laws concerning unfair terms in business-to-business contracts. For example, one option may be to use the "large" wholesale investor category (clause 39, Schedule 1 of the FMCA) as a starting point. If a business is "large" (e.g., consolidated turnover in excess of $5 million) then that business would not automatically be subject to the protections for unfair business-to-business contracts. Conversely, if the business is not "large", then those protections will automatically apply.

The FSF also submits that any such definition of businesses that fall within the scope of a new unfair contracts law would need to be sufficiently flexible to be able to address particular situations, for example where banks sold rural swaps to farm operators, many of which were large and sophisticated businesses, but which clearly did not understand the subject matter of what exactly a derivative product is and does.

One further point the FSF makes in relation to unfair contract terms whether in a business or consumer context is that New Zealand has very effective competition law in place already making it illegal for large businesses to be able to use their influence unfairly and have more bargaining power when dealing with smaller ones. The key to protecting these smaller businesses however lies in enforcing this law and the FSF therefore suggests that if a problem is identified in the course of this consultation whereby businesses feel they are being treated unfairly, it may be more of a case of the Commerce Commission using its powers to enforce existing law than a need for more legislation to define unfair contract terms.

Another point to consider in relation to the existing laws is that the Commerce Commission has now undertaken a number of reviews of standard form consumer contracts used by the telecommunications, energy retail and gym sectors for unfair contract terms ("UCTs"). In 2018, the Commerce Commission also commenced its first proceedings seeking declarations that Viagogo's standard form contracts contained UCTs. Given that the UCT regime is still bedding-in, perhaps it is too early to determine whether new laws are in fact required to address UCTs at this time (i.e. the outcome of the current Commerce Commission proceedings may provide useful guidance to set the parameters of any new laws in this area)?

**4. What types of unfair business-to-business conduct are you aware of, if any? How common is this type of conduct?**

The FSF is not aware of any unfair business-to-business conduct taking place either in the FSF's members' dealings with the businesses which contract them to provide goods and services or when they are contracting other businesses to provide them with goods or services.

Certainly, the FSF is aware of some unfair business-to-business conduct examples such as Fonterra electing to extend its creditor payment terms out to 90 days which meant businesses dealing with Fonterra having to fund themselves until they were paid. This would be a clear example of a large business using its power to unfair advantage over smaller ones but the FSF submits that such examples are not common.

The FSF also submits that credit contract providers have already been singled out in various pieces of legislation to ensure they behave fairly towards all types of customers and do not engage in oppressive conduct at any time during the course of a credit contract's lifetime including, if necessary, at any repossession. The FSF therefore sees no reason why such conduct expectations should not apply across all sectors and industries with the caveat that "business" needs to be clearly defined and a consistent definition of what constitutes a business and whether that be a small, medium or large enterprise, needs to be provided across all legislation. In this regard, see the FSF's comments in response to question 3 above on potentially using aspects of the retail/wholesale tests contained in financial markets legislation to set the types of businesses that should have the protection of any new law.

**5. What impact, if any, does this conduct have?**

In the example provided in the FSF's answer to question 4 above, the impact on suppliers to Fonterra would have included having to fund their activities via overdraft or other forms of credit whilst waiting for payment.

**6. Is government intervention to address unfair business-to-business conduct beyond existing legislative protections justified? Why/why not?**

The FSF submits that government intervention to address unfair business-to-business conduct beyond existing legislative protections would be justified only on the basis described in the answers to questions 3 and 4 above. That is to say, that the current compliance obligations that apply to the finance sector under existing legislation which prevents them from engaging in unfair conduct generally could be applied to all sectors and industries if it is deemed that there is sufficient harm being caused as a result of such poor conduct.

**7. What types of unfair business-to-consumer conduct are you aware of, if any? How common is this type of conduct?**

The FSF is aware that harm is still being caused to vulnerable consumers through the activities of some credit contract providers who ignore the law that requires them to act responsibly (the CCCFA). The reason that they are able to continue to do so even when the law clearly prevents them from so doing is because the law is inadequately enforced in the FSF's view. The FSF believes that consumer protection law in New Zealand is adequate and fit for purpose. The reason that unfair conduct from business to consumer still exists in spite of this lies with lack of enforcement not any inadequacy.

The FSF is also aware that unfair conduct does arise in other areas such as in the context of gym memberships etc. Once again, however, prevention of this type of behaviour requires enforcement of current consumer protection law.

**8. What impact, if any, does this conduct have?**

The harm caused to vulnerable consumers from unfair conduct arising out of irresponsible lending is well documented and has given rise to a further review of the CCCFA currently under way.

**9. Is government intervention to address unfair business-to-consumer conduct beyond existing legislative protections justified? Why/why not?**

The FSF refers to the answers to questions 7 and 8 above in answer to this question. The FSF further states that the Commerce Commission, whose role it is to enforce consumer protection legislation must be sufficiently well-resourced to enable it to do so.

**10. Do you agree with our proposed high-level objectives and criteria for assessing any potential changes to the regulatory framework governing unfair practices? If not, why not?**

The FSF agrees with the proposed high-level objectives as described in the Discussion Paper but questions whether there is any need for potential changes to the regulatory framework governing unfair practices as the law already exists to prevent unfair practices and the key to ensuring this law is effective lies in enforcing it.

The one further comment the FSF has would be that any assessment of potential changes could broaden the current practices required of the finance sector to apply across the board to all sectors.

**11. Should a high-level prohibition against unfair conduct be introduced? Why/why not?**

The FSF questions what evidence exists that such a prohibition is needed. New Zealand law generally applies to conduct expectations by prohibiting misleading and deceptive conduct which is quite clear in its scope. The conditions of maintaining a financial services licence in Australia include conduct obligations such as not engaging in unconscionable activity etc. The FSF believes that before New Zealand went down a similar path it would be wise to understand whether the Australian prohibitions have resulted in better outcomes for consumers and business and also what cost did it generate in order to be compliant with them.

**12. What are the advantages and disadvantages of Options 1A, 1B and 1C (refer to Annex 1 for more information)? Which option, if any, do you support?**

The FSF believes that none of the options proposed are necessary for the financial services sector due to the existing prohibition on credit contracts providers acting oppressively that is contained in the CCCFA and the fact that there are now significant numbers of examples from common law as to what constitutes that oppressive behaviour (in addition to the definition of “oppressive” in section 118 of the CCCFA and the matters for consideration in section 124 of the CCCFA). This includes where there is an imbalance of power between the contract provider and the contractee and where that imbalance has been abused.

As stated previously, however, the FSF does believe that similar obligations not to behave oppressively should be extended to non-financial sectors and industries. That said, out of the three options outlined in the discussion paper, Option 1A prohibiting “unconscionable” conduct would be the option the FSF supports most of the three options offered with the proviso that a legal meaning is attached to the word “unconscionable” for the sake of clarity.

**13. If unconscionable conduct were prohibited (Option 1A), should a definition of unconscionability be included in the statute and, if so, how should it be defined?**

Please see the answer provided for question 12 above.

**14. Is it appropriate to require businesses to act in good faith (as per Option 1C – see Annex 1)? Are there situations in which doing so could have negative economic outcomes?**

The FSF believes that it is appropriate to require businesses to act in good faith and, in fact, in many statutes they already are required to do so. For example, S25 of the Personal Property Securities Act 1999 requires: "All rights, duties, or obligations that arise under a security agreement or this Act must be exercised or discharged in good faith and in accordance with reasonable standards of commercial practice."

The requirement to act in good faith also often exists in private contracts and the requirement for parties to act in good faith in the employment law context provides the obligation for parties to consult.

"Good faith" can, however, have different meanings in different contexts so the FSF submits that any new legislative requirement for businesses to act in good faith would need to be carefullydefined as there being an absence of bad faith.

**15. Are there any other variations on Option 1 that we should consider?**

Please see the answer provided for question 12 above. The FSF has no further suggestions for other variations on Option 1 for consideration.

**16. If a version of Option 1 is selected, should it also extend to matters relating to the contract itself?**

The FSF does not believe so.

**17. Should any protection against unfair conduct apply to consumers only, consumers and some businesses (and if so, which ones), or all consumers and businesses?**

Once again, the FSF believes that the answer to this question depends largely on the definition of "consumer" and "business" and whether a similar distinction between the two might be based on the "retail/wholesale" distinction contained in the FMCA which the FSF believes would be a reasonable place to start in developing a consistent definition (see the FSF's answer to question 3). The FSF believes this concept would allow for protection of more vulnerable businesses.

Also, as noted in the FSF's answer to question 3 above, the FSF submits that the definition would need to be sufficiently flexible to be able to address particular situation, for example where banks sold rural swaps to farm operators, many of which were large and sophisticated businesses, but which clearly did not understand the subject matter of what exactly a derivative product is and does.

**18. If the UCT protections are extended to businesses, do you agree that the current consumer UCT provisions should be carried over without major changes? If not, why not?**

The FSF believes so.

**19. If the UCT protections are extended to businesses, should the FTA's "grey list" for consumer UCTs be carried over "as is"? Are there any existing examples of unfair terms that should be removed from the list, or any new examples that should be added?**

The FSF believes that the FTA's consumer UCT grey list is reasonable and therefore could be applied to businesses. The issue with this, however, goes back to the point the FSF has previously made as to the need for a consistent definition across all statutes as to what exactly a "business" is (and whether large sophisticated businesses should be carved-out from any new laws).

**20. Should the protections against UCTs apply to consumers only (as at present), consumers and some businesses (and if so, which ones?), or all consumers and businesses?**

Please refer to the answer provided to question 19.

**21. If the protections against UCTs are extended to businesses, should a transaction value threshold be introduced, above which the protections do not apply? If so, what should the threshold be?**

The FSF believes that the answer to this question also depends on getting the definition of what exactly constitutes a "business" right. A threshold would be hard to apply so a more appropriate way to protect businesses from UCTs would be to appropriately define what is and is not a business to which the UCTs are being extended.

**22. Should there be penalties for breaching any new provisions regarding UCTs, and should there be civil remedies available, even if unfair terms have not previously been declared by a court to be unfair? How should any penalties and remedies be designed?**

The FSF suggests that some common law on potential penalties that could be applied should any breaches of new provisions regarding UCTs occur that have arisen out of decisions regarding financial contracts already exists.

The FSF also submits that potential penalties for non-compliance should be consistent with the penalty framework under similar legislation. For example, if the oppressive prohibition in the CCCFA is carried over to other industries, it is submitted that consequences for non-compliance should also be carried over (which, broadly speaking, means that a court would have the power to re-open that contract and make any orders that it thinks necessary – see section 127 of the CCCFA).

In addition, it would be important for the Commerce Commission (or any other agency charged with the enforcement of any new legislation) to be adequately resourced to be able to communicate with businesses regarding best practices for compliance, monitor compliance and enforce the new laws.

**23. Are there other options to address unfair conduct or unfair contracts that we should consider? If so, what are these?**

The FSF cannot suggest any other options to address unfair conduct or unfair contracts than have already been put forward in this submission.

**24. Do you have a preferred options package? If so, which is your preferred package, and why?**

The FSF would prefer that, at least as far as credit contracts providers are concerned, the status quo was largely allowed to remain. As previously suggested in this submission, the provisions against oppressive conduct that apply to credit contracts providers could be given a much wider application so that all sectors are covered by them in which case none of the options presented in the Discussion Paper would be required.

If it still considered that something does need to be done to protect businesses from these kinds of practices, the FSF's preferred option is Option 1A to prohibit unconscionable conduct. However, this comes with the proviso that both "unconscionable" and "business" need to be properly defined in law and that, in particular the definition of what is a "business", should be consistent with other legislation.

Further, as previously stated in this submission, the FSF also believes that the Commerce Commission needs to be adequately resourced to be able to enforce existing law and any further legislation arising out of this consultation.

**25. Do you agree with our assessment of the impact of each package against the criteria? If not, why not? Do you have any further evidence on the costs and benefits of this option?**

The FSF has nothing further to add other than what has already been said in this submission.

Thank you once again for the opportunity for the FSF to submit on these proposals. Please do not hesitate to contact me if you have any further questions.

Lyn McMorran
EXECUTIVE DIRECTOR

## Appendix A
## FSF Membership List as at 20 December 2018

| Debenture Issuers - (NBDT)<br>Non-Bank Deposit Takers | Vehicle Lenders | Finance Company<br>Diversified Lenders | Credit Reporting<br>Other | Insurance | Affiliate Members |
|---|---|---|---|---|---|
| Rated<br>Asset Finance (B)<br><br>Non-Rated<br>Mutual Credit Finance<br>Gold Band Finance<br>➢ Loan Co | BMW Financial Services<br>➢ Mini<br>➢ Alphera Financial Services<br>Branded Financial Services<br>Community Financial Services<br>European Financial Services<br>Go Car Finance Ltd<br>Honda Financial Services<br>Mercedes-Benz Financial<br>Motor Trade Finance<br>Nissan Financial Services NZ Ltd<br>➢ Mitsubishi Motors Financial Services<br>➢ Skyline Car Finance<br>Onyx Finance Limited<br>Toyota Finance NZ<br>Yamaha Motor Finance<br><br>Leasing Providers<br>Custom Fleet<br>Fleet Partners NZ Ltd<br>ORIX NZ<br>SG Fleet<br>Lease Plan | L & F Ltd<br>➢ Speirs Finance<br>➢ YooGo<br>Avanti Finance<br>Caterpillar Financial Services NZ Ltd<br>CentraCorp Finance 2000<br>Finance Now<br>➢ The Warehouse Financial Services<br>Flexi Cards<br>Future Finance<br>Geneva Finance<br>Home Direct<br>Instant Finance<br>➢ Fair City<br>➢ My Finance<br>John Deere Financial<br>Latitude Financial<br>Pioneer Finance<br>➢ Personal Finance<br>South Pacific Loans<br>Thorn Group Financial Services Ltd<br>Turners Automotive Group | Equifax (prev Veda)<br>Centrix<br><br>Debt Collection Agencies<br>Baycorp (NZ)<br>Illion (prev Dun & Bradstreet (NZ) Limited | Autosure<br>Protecta Insurance<br>Provident Insurance Corporation Ltd<br>Southsure Assurance | AML Solutions<br>Buddle Findlay<br>Chapman Tripp<br>EY<br>Finzsoft<br>KPMG<br>Paul Davies Law Ltd<br>PWC<br>Simpson Western<br>FinTech NZ<br>HPD Software Ltd<br>Receivables Management<br>Experian<br><br>Total : 57 members |