NEW ZEALAND LAW SOCIETY

NZLS EST 1869

Fair Trading Amendment Bill

27/03/2020

Submission on the Fair Trading Amendment Bill

1 Introduction

1.1 The New Zealand Law Society|Te Kāhui Ture o Aotearoa (**the Law Society**) welcomes the opportunity to comment on the Fair Trading Amendment Bill (**the Bill**).

1.2 The Law Society's comments on the Bill focus on the introduction into the Fair Trading Act 1986 (**the Act**) of a prohibition against "unconscionable conduct". The Law Society's key concern is that more certainty is needed about the type of conduct that can properly be regarded as breaching the prohibition.

1.3 The Law Society does not seek to be heard but is happy to engage further with the select committee or officials if that would be of assistance.

2 Prohibition against "unconscionable conduct": new sections 7 and 8

Unfair commercial practices – "unconscionable conduct"

2.1 The Bill's policy objective is to preclude 'unfair commercial practices', including "unconscionable conduct" – which is referred to in the Explanatory Note as "serious misconduct that goes far beyond being commercially necessary or appropriate".[1]

2.2 Clause 6 of the Bill inserts new sections 7 and 8 of the Act, prohibiting "unconscionable conduct in trade" and setting out matters the courts may have regard to in determining whether conduct is unconscionable.

2.3 New section 7 stipulates that the prohibition against unconscionable conduct in trade applies "*whether or not … a particular individual is identified as disadvantaged, or likely to be disadvantaged, by the conduct*" (s.7(2)(a), emphasis added).

2.4 New section 8 lists a number of factors the courts may have regard to when deciding whether conduct is unconscionable, such as:

- "the relative bargaining power of the person engaging in the conduct (**the trader**) and any person … disadvantaged, or likely to be disadvantaged, by the conduct (**an affected person**)" (s.8(1)(a));
- "the extent to which the trader and an affected person acted in good faith" (s.8(1)(b));
- "whether, *taking account of the particular characteristics and circumstances of an affected person*, the affected person or the affected person's representative was reasonably able to protect the affected person's interests" (s.8(1)(c)); emphasis added).

2.5 The Bill makes it an offence under section 40(1) of the Act to contravene the prohibition on unconscionable conduct in trade, with significant consequences that include maximum fines of $200,000 (for individuals) and $600,000 (for body corporates).[2]

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1 Fair Trading Amendment Bill 2020, 213-1, explanatory note at p1.

2 See note 1, at p2: Existing provisions in the Act dealing with civil proceedings and remedies (such as injunctions, refunds, damages, and having contract terms altered or declared void) also apply.

The threshold at which conduct is deemed "unconscionable"

2.6 There is currently no statutory prohibition in New Zealand against 'unconscionable' conduct, but the concept of unconscionability has developed in case law and has been applied where the courts have considered it inequitable to allow a party to enforce contractual rights against another party. As noted in the regulatory analysis supporting the Bill, three essential features justifying such intervention are that:

- the weaker party has a qualifying disability (e.g. age, infirmity, difficulty understanding English);
- the stronger party has knowledge (actual or constructive) of this disability; and
- the stronger party took advantage of this disability to extract a benefit from a transaction.[3]

2.7 However, under the Australian statutory prohibition, which officials consider is "relatively effective in addressing conduct which is particularly unfair and egregious", conduct can be found to be unconscionable "even if there is *no conscious targeting* of a vulnerable party".[4] The Bill is based on the Australian model:[5] this is reflected in the proposed new sections 7 and 8, which require the courts to consider the "particular characteristics and circumstances" of the affected person (s.8(1)(c), *regardless* of whether the trader has identified that the person is "disadvantaged, or likely to be disadvantaged" by the conduct (s.7(2)(a); emphasis added).

2.8 The Law Society questions whether this is justified. For a statutory prohibition backed by serious criminal consequences, we consider that some element of culpability – i.e. that the trader knew, or ought to have known, that the person was vulnerable and took advantage of that vulnerability – should be required. The Legislation Guidelines state in relation to the creation of criminal offences that –

> 9.1 Offences must be defined clearly so that people know what is and what is not prohibited. Therefore, it is necessary to consider exactly what conduct (called the *actus reus*) is prohibited by a criminal offence. The description of the conduct should be precise and rationally connected with the harm targeted by the policy objective. An imprecise statement of the prohibited conduct may lead to inconsistent enforcement of the law, uncertain application of the law, unintended changes in behaviour, or failure to preclude conduct that it was intended to prohibit.[6]

2.9 It is notable that the alternative option of prohibiting "oppressive conduct" was preferred by officials. The reasons for this are persuasive and are set out in full below. The Law Society recommends that the committee consider this alternative option and obtain further advice from officials.

Regulatory analysis of the options

2.10 The RIS records that the government decided to proceed with Option 1A (a prohibition against "unconscionable conduct in trade") on the basis that this will support alignment with Australia

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3 *Protecting business and consumers from unfair commercial practices*, Regulatory Impact Analysis (**RIS**) dated 20 June 2019, MBIE, at p10, emphasis added.

4 RIS (note 3), at p24, emphasis added.

5 RIS, at p38: "on the basis that Option 1A [prohibition against unconscionable conduct] will support alignment with Australia and allow New Zealand to draw on Australian case law".

6 Legislation Guidelines: 2018 edition, at Chapter 24.

and allow New Zealand to draw on Australian case law, despite officials' reservation that it is "relatively uncertain how the [New Zealand] courts will interpret 'unconscionable'".[7]

2.11 Officials preferred Option 1B (prohibiting "oppressive conduct") because it aligns with the definition in the Credit Contracts and Consumer Finance Act 2003,[8] and the existing New Zealand case law on the nature of oppressive conduct could reduce uncertainty as to the type of conduct that will breach the prohibition.

2.12 The Law Society agrees with the reservations expressed by officials about Option 1A and their preference for Option 1B:

> As outlined earlier in this RIS, we think there is a case for introducing additional protections for both businesses and consumers against unfair conduct. Options 1A and 1B would both be targeted at similar conduct, and we think that either option would provide net benefits relative to the status quo.
>
> We prefer Option 1B on the basis of Criterion 1: *Consumers are protected from high levels of detriment and practices which unduly impact on their ability to confidently participate in markets*, Criterion 2: *Businesses are protected from practices which unduly impact on their ability to confidently participate in markets*, and Criterion 4: *The law is predictable for businesses and compliance costs are reasonable*.
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> Both options are targeted at similar conduct, and both would involve an element of uncertainty as to the threshold before conduct would be in breach of the prohibition. However, we think the potential for uncertainty associated with Option 1A is higher than Option 1B. This because there is an established body of case law (albeit restricted to credit contracts and related transactions) about the meaning of oppression, **which appears to strike a suitable balance between prohibiting conduct that is grossly unfair, while not unnecessarily intervening in everyday, reasonable, commercial conduct**. In contrast, because the case law related to unconscionability relates to the more narrow equitable doctrine, rather than that intended by a legislative prohibition, we think that there is a risk that prohibiting unconscionable conduct could lead to the courts interpreting the prohibition too narrowly.
>
> We also think that the reference to factors such as 'reasonable standards of commercial practice' under an oppressive conduct prohibition offers more guidance to businesses than reference to factors such as 'conscience' and the 'norms of society' that could be referenced under an unconscionable conduct prohibition (if Australian case law is followed). This is strengthened by the fact that evidence as to what reasonable standards of commercial practice are is likely to influence a court's findings as to whether conduct is oppressive.[9]

2.13 The Law Society also notes that while there are benefits to being able to draw on Australian case law, the approach taken by the Australian courts will not necessarily be consistent with what the

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7 RIS, at p38 and p32.

8 RIS, at p33. Under this Act, the term "oppressive" means *oppressive, harsh, unjustly burdensome, unconscionable, or in breach of reasonable standards of commercial practice*.

9 RIS, at p33, bold emphasis added.

Bill seeks to achieve. A recent decision of the Australian High Court,[10] a summary of which is attached to this submission, illustrates the difficulties courts can face in determining whether conduct is unconscionable, and provides an example of a narrow interpretation which appears to be inconsistent with the policy intent of this Bill.

3 <u>Minor drafting correction</u>

Clause 7: Extension of unfair contract terms provisions to standard form small trade contracts

3.1 There is a possible ambiguity arising from use of the pronoun "it", referring to the "small trade contract", in new section 26C(1)(c) and we therefore suggest the following minor correction for clarity:

> *"(c) it does not comprise or form part of a trading relationship that exceeds the annual value threshold when ~~it~~ <u>the relationship</u> first arises*."

Herman Visagie
NZLS Vice President
27 March 2020

Attachment: summary of *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18

[10] *Australian Securities and Investments Commission v Kobelt* [2019] HCA 18.

Australian Securities and Investments Commission v Kobelt [2019] HCA 18 illustrates the difficulties the courts can face when assessing whether the threshold of unconscionability has been reached.

Mr Kobelt provided a system of "book up" to his customers, most of whom were Aboriginal residents of the APY Lands, which allowed them to purchase goods and second-hand motor vehicles on credit. In return, Mr Kobelt required his customers to provide him with their debit cards, PINs and details of their income, which he then used to withdraw all, or nearly all, of the customer's money from their bank account on or around the day they were paid.

The Federal Court had found at first instance that Mr Kobelt's system of providing book up (which included the requirement to hand over debit cards and PINs, and the removal of funds from bank accounts on pay days) was unconscionable.

However, in the High Court, four judges (Kiefel CJ, Bell, Keane and Gageler JJ) found that Mr Kobelt's book up system was not unconscionable. The remaining three judges (Nettle, Gordon and Edelman JJ) dissented.

Chief Justice Keifel and Justice Bell focused on a narrow interpretation of unconscionable conduct, requiring that the trader must have exploited or otherwise taken advantage of the disadvantage of their customers. They found that principally because the customers entered into the credit arrangements 'voluntarily' and there was limited evidence of dissatisfaction with the arrangement, and so they felt it could not be established "… *that the respondent exploited his customers' socio-economic vulnerability in order to extract financial advantage from them*" (per Keane J at [115]).

In contrast, the minority found that unconscionable conduct was made out. Justices Nettle and Gordon found that Mr Kobelt did unconscionably take advantage of his customers' vulnerability, stating:

> "… *it is because a transaction that is <u>voluntarily</u> entered into by someone under a special disadvantage that unconscionability, including statutory unconscionability, developed, in order to ensure that persons who are vulnerable and unable to protect their own interests are not the victim of conduct by a stronger party in unconscientiously taking advantage of that vulnerability*" (per Nettle and Gordon JJ at [238]).

Similarly, Justice Edelman also said it was wrong to conceive that the customers 'chose' the system of credit, stating that "*the conclusion of unconscionability cannot be avoided by pointing to this so-called 'choice' between Mr Kobelt's system of credit and no credit at all*" (per Edelmann J at [313]). This reflects that there were no other options to purchase goods and services, leaving book up as the last resort.