

Review of the Redress and Enforcement Provisions of Consumer Protection Law

International Comparison Discussion Paper

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Foreword

Creating an environment where consumers can transact with confidence is the ultimate goal of consumer protection policy. What this means in practice is that consumers should get what they reasonably expect from a purchase and, if not, have access to redress.

Transacting with confidence is not just important to the individual consumer, it is also essential for a thriving, innovative and sustainable economy.

In order to create an environment where consumers can transact with confidence, the government provides information and establishes market rules (including setting standards and having consumer law setting out rights and protections) and provides mechanisms for their enforcement (including access to redress).

The two overarching pieces of legislation setting out consumer rights and protections are the Fair Trading Act 1986 (FTA) and the Consumer Guarantees Act 1993 (CGA).

It is important on a regular basis to assess whether the desired outcomes of our consumer protection laws are being achieved. To better understand how effective the enforcement of the FTA and the CGA are in practice, the Ministry of Consumer Affairs is undertaking a review of the redress and enforcement provisions of these key consumer protection laws.

One way of monitoring whether our consumer protection laws are delivering the best possible outcomes is to compare our laws with those in similar overseas jurisdictions. This approach provides not only a type of benchmarking exercise but also ensures we are aware of current international consumer policy trends.

This discussion paper summarises the redress and enforcement provisions found in consumer protection legislation in other similar jurisdictions overseas that are different from those in the FTA and CGA and considers whether their availability would be beneficial to improving the environment for consumers to transact with confidence.

I invite businesses and consumers to consider the proposals and make submissions to the Ministry of Consumer Affairs on whether you think the proposals will enhance the effectiveness of consumer protection legislation in this country.

Hon Judith Tizard
Minister of Consumer Affairs

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Introduction

The Fair Trading Act 1986 (FTA) and the Consumer Guarantees Act 1993 (CGA) establish a regulatory framework which protects consumers from unfair business practices and protects businesses who comply with the legislation from unfair competition. For example, the legislation does this by prohibiting misleading and deceptive conduct and false representations. By prohibiting such practices, businesses can compete fairly against each other on price and on the basis of any extra services that they may choose to provide to consumers.

The FTA and the CGA sit alongside other legislation such as the Commerce Act 1986 and the Securities Act 1978, which aim to promote competitive and fair markets, the efficient allocation of resources and, overall, improved consumer well-being and a well-functioning marketplace.

If businesses are not deterred from breaching the consumer protection legislation, this can impact on consumer confidence. When consumers are not confident they may delay making transactions or may choose not to purchase if they perceive that the risks are too high. Consumers can incur extra costs by spending considerable amounts of time gathering information, by paying more for a good or service in an attempt to avoid a bad deal and by continuing to purchase from the same supplier in an attempt to avoid the potential risks associated with switching suppliers even though another supplier may offer a better deal. When consumers lose confidence in this way they may incur additional costs and competition and market efficiency will be adversely affected by consumers transacting less and suffering from inertia.

The overarching desired outcome for consumer protection policy in New Zealand is an environment where consumers can transact with confidence. Transacting with confidence in this context means that consumers' reasonable expectations of transactions will be met. For this to happen, businesses need to comply with the legislation. In those instances where a transaction goes wrong then consumers have to have ready access to appropriate redress.¹

For consumer protection legislation to be effective, it needs to protect both consumers and honest businesses from failures to meet quality guarantees, unsafe products and misleading or deceptive conduct. Enforcement tools and penalty provisions that encourage compliance and act as a deterrent are required. According to the pyramid theory of responsive regulation,² compliance is best secured by the use of persuasion and negotiation techniques. To be effective, however, these techniques have to be supported by a range of escalating sanctions which can be applied or used depending upon the level of cooperation by the business and the

¹ An intervention logic that identifies the intermediate outcomes that would need to be achieved and the assumptions that are being made for the desired policy outcome to occur has been developed and is outlined in *Review of the Enforcement of Consumer Protection Law: An Initial Think Piece* [www.consumeraffairs.govt.nz/policylawresearch/enforcement-review/], July 2005.

² The pyramid theory of responsive regulation is sometimes referred to as the enforcement pyramid.

seriousness of the contravention.³ When a range of sanctions is available, lower level enforcement measures are more effective. The threat of more severe forms of punishment encourages businesses to comply.

Effective consumer protection legislation also depends on consumers and businesses having knowledge of their rights and obligations under the legislation and their ability to apply this knowledge when they are transacting and to their businesses.

The Ministry of Consumer Affairs (MCA) is reviewing the effectiveness of the redress and enforcement provisions in the FTA and the CGA conducted as part of the government's ongoing monitoring of its legislation in order to assess how effective it is in practice in achieving desired outcomes.

As part of this review, MCA has undertaken a survey of consumers and is currently surveying businesses in order to gain an understanding of their experience, awareness and understanding of consumer rights in the marketplace.⁴

The consumer survey, which involved a nationwide random sample of 1,000 people aged 18 years and over, found that consumers are, on balance, generally confident with the cross section of businesses they deal with. Consumers do not on the whole expect to experience frequent or wide-ranging risk. In other words, consumers perceive the New Zealand marketplace as a relatively benign trading environment.

This is not to say that problems do not arise. From the consumer's point of view, whether correctly or incorrectly interpreted, adverse effects are quite common. However, they rarely have an economic impact and many are readily resolved by the consumer approaching the trader.

Consumer law relies to a significant extent on consumers taking action for themselves. The consumer survey shows that this seems to be working well and, accordingly, the underlying principles of our consumer protection legislation are sound. An important part of the consumer law regime is also the enforcement tools that are available to the enforcement agencies (in most cases the Commerce Commission). To identify whether all the best available redress and enforcement tools are available in our consumer legislation, MCA has undertaken an international comparison. This is akin to a benchmarking comparison.

This discussion paper compares the redress and enforcement provisions of the FTA and the CGA with those found in consumer protection legislation in Australia, Canada, the USA and the United Kingdom, that:

- forbid the production and selling of unsafe products;

³ A more detailed explanation of the enforcement pyramid is provided in *Review of the Enforcement of Consumer Protection Law: An Initial Think Piece* [www.consumeraffairs.govt.nz/policylawresearch/enforcement-review/], July 2005.

⁴ The consumer survey, *National Consumer Survey of Awareness and Experience of Consumer Legislation* [www.consumeraffairs.govt.nz/policylawresearch/research/awareness/], was conducted during June-July 2005 by National Research Bureau.

- prohibit behaviour that is misleading or deceptive; and
- set out redress, enforcement and penalty provisions.

Where differences in the prohibitions and redress and enforcement provisions between the New Zealand legislation and the overseas legislation have been identified these have been examined in more depth and the advantages and disadvantages of adopting such provisions are discussed, always keeping in mind whether new or additional provisions in the FTA or the CGA would improve the effectiveness of the legislation and assist the Commerce Commission to act more effectively and efficiently when a business appears to be breaching the legislation. By being able to act quickly, the potential harm to consumers and other businesses can be reduced.

Structure of This Document

This discussion paper is divided into five main parts. The first part provides background on New Zealand's consumer protection legislation. There is discussion of the purpose of the legislation and the prohibitions. The redress and enforcement provisions in the FTA and the CGA are then summarised. Also summarised is how the legislation enables consumers to get redress and the enforcement action that can be taken and by whom under the FTA and the CGA.

Part two of the discussion paper provides a summary comparison of the prohibition, redress and enforcement provisions found in the FTA and the CGA with the consumer protection legislation found in the selected overseas jurisdictions.

There are provisions in the consumer protection legislation in the other jurisdictions that may allow consumers to transact with more confidence, protect the honest business, and assist the Commerce Commission in its enforcement role. Part three discusses the advantages and disadvantages of adopting these provisions and proposes that the FTA be amended to include them.

The comparison of consumer protection legislation in the other jurisdictions also identified provisions that, following analysis, are not proposed to be adopted into New Zealand's consumer protection law. These provisions are discussed in part four.

MCA is calling for submissions on this document. The submission process is outlined in part five.

Executive Summary

The redress and enforcement provisions in New Zealand's Fair Trading Act 1986 (FTA) and the Consumer Guarantees Act 1993 (CGA) have been compared with those found in consumer protection legislation in Australia, Canada, the USA and the United Kingdom.

Overall, the FTA and the CGA contain prohibitions and redress and enforcement provisions that are very similar to those that are available in consumer protection legislation in the comparison jurisdictions.

Whilst there are no significantly different approaches in the overseas legislation, analysis has indicated that there may be some additional prohibitions, investigation and enforcement tools and penalties that may strengthen the FTA in terms of achieving the desired outcomes for consumers and businesses.

It is proposed that amendments to the FTA be considered to provide for:

- Unfair terms in consumer contracts prohibition;
- Product safety warning notices and powers of investigation;
- Cease and desist orders;
- Substantiation notices;
- Court enforceable undertakings;
- Compulsory interview powers; and
- Banning orders.

Including these prohibitions and redress and enforcement provisions in the FTA should assist the Commerce Commission to act more effectively and efficiently when it believes that a contravention has occurred.

The proposals should provide better protection for consumers and thereby allow them to transact with more confidence and should enable compliant businesses to compete fairly.

Part 1 – Summary of New Zealand’s Consumer Protection Law

The Fair Trading Act 1986

The Fair Trading Act (FTA) prohibits certain conduct and practices in trade, provides for the disclosure of consumer information relating to the supply of goods and services and promotes product safety. The FTA is substantially based on Part V of the Australian Trade Practices Act 1974.

Part 1 - Prohibitions

Under Part 1 of the FTA, there are three main types of prohibitions:

- misleading and deceptive conduct;
- false representations; and
- unfair practices.

Misleading and Deceptive Conduct

Sections 9 to 12 of the Act cover all conduct that is misleading or deceptive or is likely to mislead or deceive. Section 9 covers misleading and deceptive conduct generally, Section 10 covers misleading conduct in relation to goods, section 11 covers misleading conduct in relation to services, and section 12 covers misleading conduct in relation to employment.

False Representations

Section 13 of the Act gives a list of specific areas in which representations must not be false or misleading. The distinction between section 9 (misleading and deceptive conduct generally) and section 13 (false or misleading representations) is deliberate. Contravention of section 13 can give rise to a criminal as well as civil liability whereas only a civil charge is possible under section 9.

Section 14 outlines prohibitions for false representations regarding the sale of land. A breach of this section is a criminal offence but a breach of subsection 2 (section 14(2)) is a civil offence only.

The Act also places prohibitions on certain conduct regarding trademarks. Civil and criminal sanctions apply.

Unfair Practices

The various unfair practices which are prohibited under the Act are:

- Offering gifts and prizes without the intention of providing them

- Bait advertising⁵
- Referral selling⁶
- Demanding or accepting payment without intending to supply as ordered
- Misleading representations about certain business activities
- Harassment and coercion
- Pyramid selling schemes.

Part 2 – Consumer Information

Sections 27 to 28 of the FTA provide for regulations creating consumer information standards for goods and services. These relate to the type of information which must be disclosed and the way that information is to be disclosed. Currently there are four consumer information standards, covering:

- country of origin clothing and footwear;
- fibre content labelling;
- care labelling; and
- supplier information notices (SINs) for used vehicles.

Part 3 – Product Safety

Section 29 provides for regulations prescribing certain product safety standards.

There are currently 6 product safety standards relating to:

- children's toys
- cigarette lighters
- children's nightwear and limited daywear having reduced fire hazard
- household cots
- pedal bicycles
- baby walkers.

⁵ Bait advertising is advertising that a product or service is available when it actually cannot be supplied or where reasonable quantities cannot be supplied.

⁶ Referral selling is where a business offers a potential customer a reward if they supply the names of other potential customers. If no sale is made to the referred customers, the original customer does not get their reward.

These standards establish particular requirements that must be met, usually by referring to Australian/New Zealand Standards.

Under section 31, the Minister can declare goods to be unsafe if the good may cause an injury to any person. Such notices are effective for 18 months.⁷ If goods do not comply with product safety standards, or may cause injury to any person and the trader has not recalled the goods, the Minister may compulsorily require the goods to be recalled (section 32).

Part 4 – Safety of Services

Section 34 provides for regulations prescribing safety standards in respect of services. There are no safety of services standards currently in force.

Part 5 – Enforcement and Remedies

The FTA is enforced by the Commerce Commission. Individuals and corporations can also take action under the Act.

Civil proceedings and criminal prosecutions can be taken. However, in some cases only civil proceedings can be taken. This includes breaches of section 9, which prohibits misleading conduct in trade and which is the most frequently litigated section of the Act. As well, the Disputes Tribunal has no jurisdiction for breaches under this section. Civil remedies include injunctions, orders for corrective advertising (only available to the Commerce Commission), private actions and other compensatory orders, depending on the jurisdiction of the Court.

Under the FTA offences are generally strict liability, that is, a person is held responsible for damages resulting from their actions regardless of their level of fault.

Breaches of the FTA can lead to civil or criminal liability with a fine of up to \$60,000 for individuals. If the trader is a body corporate they may be liable for a fine of up to \$200,000. If there is more than one offence for the same breach, then total fines imposed cannot exceed the maximum.

The one exception to the maximum fine provision relates to pyramid selling. Pyramid selling⁸ is a criminal offence with a fine of up to a maximum of \$200,000. If a person is convicted of pyramid selling, that person can be required to repay any commercial gain made from their dealings in addition to any fine.

⁷ The period of the notice can be extended for a specified period or indefinitely.

⁸ The main characteristic of a pyramid selling scheme is that earning money and gaining promotion within the scheme depends primarily on recruiting new people to the scheme, and those new people recruiting more people into the scheme, and these new people recruiting more people, and so on...

Pyramid schemes are unfair trade practices because they are likely to be unfair to most participants in the scheme, the rewards for those at the top come from those below, and because eventually it will become impossible to recruit the number of people needed to produce reasonable financial rewards to participants.

The Court has other powers following a contravention of the Act. It may declare a contract void or vary its terms, order money or property be returned to the person who suffered loss, order goods be repaired or supplied, or order services be supplied.

The limitation period for prosecuting offences is 3 years after the matter giving rise to the contravention was discovered or ought reasonably to have been discovered.

Part 6 - Miscellaneous Provisions

The FTA gives the Commerce Commission powers of entry, search and seizure, and inspection as well as the power to require the supply of information or documents. Employees of the Commerce Commission can apply for a warrant to search premises. A warrant may be issued subject to some conditions, including obligations and powers of the person executing the warrant.

Refusing to co-operate with a search, refusing to provide documentation, or knowingly providing false or misleading information is an offence, although with lower fines than those associated with breaching other parts of the FTA (up to \$10,000 for an individual and \$30,000 for a body corporate).

The Consumer Guarantees Act 1993

The Consumer Guarantees Act 1993 (CGA) generally has the purpose to provide certain degrees of protection to consumers regarding the supply of goods and services. It sets out a number of guarantees concerning the supply of goods and services and requires traders and manufacturers to provide remedies to consumers when these guarantees are not met. The CGA is based on the Saskatchewan⁹ consumer protection legislation (prior to 1997) and New Zealand case law prior to 1993.

Redress in the Consumer Guarantees Act

Under the CGA, consumers have the right of redress when:

- the goods do not meet a guarantee of acceptable quality (section 6);
- the good is not fit for the particular purpose that the trader represented it to be, or for the purpose for which the consumer makes clear they are buying the product (section 8);
- the goods do not correspond to the description by which they are supplied by (section 9);
- the goods do not correspond to the sample or demonstration model on which the sale was based (section 10);

⁹ A province in Canada.

- the consumer pays the trader more than a reasonable price for the goods (subject to other riders) (section 11);
- under Part III, the manufacturer fails to ensure that facilities for repair of the goods and supply of parts for the goods are available for a reasonable period after the goods were supplied (section 12); and
- under Part III, the manufacturer does not stand by their express guarantee (which is binding) (section 13).

When goods fail to comply with any of the guarantees set out above, the consumer has the right of redress against the trader (given by section 16 and outlined below). There is one exception to this – when the manufacturer instead of the trader has breached the guarantee of acceptable quality. In this situation the consumer has no right of redress against the trader, but does against the manufacturer. In all other cases, there is a right of redress against the trader even if they are unaware of such a failure. In other words, the guarantee provisions impose strict liability. Traders are expected to disclose any defects in the goods to the consumer if known.

The right of redress against the trader applies not only to the original consumer, but anyone (as long as that person meets the definition of consumer) who acquires the goods from or through the consumer.

Repair, Replace or Refund

If a good is faulty (i.e. does not comply with the CGA guarantees provided under sections 5, 6, 7, 8, 9 or 10), the trader must remedy the failure.¹⁰ If the failure can be repaired, the trader must repair the goods. The consumer may require the trader to remedy the failure within a reasonable time.

If the failure cannot be repaired or is of substantial character, the trader must replace the goods with an identical or superior type, or refund the purchase price. The consumer can choose which of these remedies is most acceptable to them.

In the case of a failure that is of substantial character and can be remedied, the consumer has two choices:

- to require the failure to be remedied; or
- to reject the goods.

If a trader does not remedy the problem or takes an unreasonable time to remedy the problem, the consumer can have the failure remedied elsewhere and charge all reasonable costs to the trader. The consumer must give the trader an opportunity to remedy the defects before taking the goods to someone else to fix, otherwise the consumer loses the right to seek reimbursement of costs from the original trader.

¹⁰ This does not apply to an express guarantee, i.e. a written manufacturer's guarantee, as this is covered under Section 25 (d) of the CGA which outlines the rights of redress against the manufacturer.

Alternatively, the consumer can choose to reject the goods and seek a refund or replacement goods.

Rejection

Consumers cannot reject the goods after they have been satisfactorily repaired.

Where consumers reject the goods, they have to notify the trader that they reject the goods and give the reasons for the rejection. The consumer is also obliged to return the goods to the trader unless the cost of doing so is substantial.

A consumer loses the right to reject goods if the right is not exercised within a reasonable period of time.

The right of rejection is also lost if:

- the consumer has disposed of the good(s) or if they have been lost or destroyed while in the possession of a person other than the trader or an agent of the trader;
- the goods are damaged after delivery for reasons not related to the condition of the goods at the time of supply;
- the goods have been attached or incorporated in any property and cannot be isolated without damage.

Right of Redress against the Manufacturer

Part III sets out the rights of redress for a consumer against a manufacturer. These rights are not as extensive as those against the trader and are mainly restricted to claiming damages for any reduction in the value of the goods below the purchase price. The consumer has rights when the goods fail to comply with the CGA guarantees such as acceptable quality, access to repairs and spare parts, description of the goods, and express guarantee of the manufacturer. As with traders, the right of redress against the manufacturer applies not only to the original consumer, but anyone (as long as that person meets the definition of consumer) who acquires the goods from or through the consumer.

There are some exceptions to seeking redress from the manufacturer. The manufacturer cannot be liable for:

- a breach of guarantee of quality if that guarantee was not made by the manufacturer;
- a breach that is due to a cause independent of human control occurring after the goods have left the control of the manufacturer;
- a breach that arises only as a result of the price being charged by the trader that is higher than the recommended retail price (or average price).

Consequential Loss

In all cases where a consumer has a right of redress, they also have the right to obtain damages for any loss or damage resulting from the failure which was reasonably foreseeable as likely to result from the failure. Damages can be claimed whether or not the failure was remedied, and whether or not the failure was of a substantial character.

If Direct Remedies Don't Work

The legislation does not allow for enforcement under the CGA to be carried out by the Commerce Commission or any other government or third party agency. The consumer may initiate civil legal action if the remedies are not followed through. The Disputes Tribunal, District Court or the High Court may hear claims for costs, damages, or for a refund payable under the Act. There is one exception to the consumer-driven redress rule: if a trader attempts to contract out of the obligations imposed by the Act, they may be committing an offence under s 13(i) of the Fair Trading Act (for example, a sign in a shop that states that refunds are not available). The offending trader can then be prosecuted by the Commerce Commission.

Exercising Consumer Rights and Getting Redress under the Fair Trading Act and the Consumer Guarantees Act

New Zealand consumer protection legislation relies to a large extent on consumers taking action for themselves. No enforcement agency is responsible for enforcing the CGA and while the Commerce Commission has enforcement responsibilities with respect to the FTA, it is only able to investigate a small percentage of the complaints it receives. When the Commerce Commission takes action against a trader, its primary goal may be not to secure redress for the individual consumers detrimentally affected by the breach.¹¹

This means that when a consumer does not get what they expect from a transaction or when a transaction goes wrong, they are largely responsible for pursuing their own remedy. Consumers may decide that it is not worth their while trying to put a transaction right. This may occur, for example, when the price paid for a good is relatively low or when a consumer decides that their best course of action is to try and avoid a similar transaction occurring in the future and therefore “vote with their feet” (for example, they decide not to return to a restaurant where they were dissatisfied with a meal or service that they received). Where consumers decide to take action, they are required in the first instance to try and get redress from the trader concerned.

If consumers cannot resolve the matter with the trader there are a number of options that a consumer can pursue. The consumer may at this stage decide not to take any further action or may try and resolve the matter by, for example, contacting the head office, a trade association to which the trader belongs, a specific complaints body if there is one (for example, the Electricity and Gas Complaints Commissioner) or take

¹¹ In a recent court case, however, the Commerce Commission dropped a prosecution after the company agreed to refund \$54,000 to customers who were incorrectly billed.

the matter to the Disputes Tribunal. Consumers can take matters to the District Court but because of the costs involved it is unusual for consumers to do this. Court cases involving consumer protection legislation are usually instigated by businesses or the Commerce Commission.

Part 2 - Summary Comparison with Overseas Jurisdictions

Introduction

This part of the discussion paper compares the prohibitions and the redress and enforcement provisions in the Fair Trading Act (FTA) and the Consumer Guarantees Act (CGA) with those that are found in consumer protection legislation in Australia, the United Kingdom, Canada and the United States of America. All four jurisdictions were chosen because of common consumer protection principles and policy to those in New Zealand. Australia and Canada were also chosen because the drafting of New Zealand's consumer protection legislation was substantially informed by their legislation. The misleading and deceptive conduct and product safety provisions found in the FTA largely mirror those found in Australia's Trade Practices Act. The CGA is based on the Saskatchewan Consumer Protection Act (prior to 1997).

This comparison has been done in order to identify whether

- other similar jurisdictions' approaches to consumer protection policy have diverged since referenced in the drafting of the FTA and the CGA, in 1986 and 1993 respectively; and
- different prohibitions and provisions to protect consumers and honest businesses have been adopted since the enactment of the FTA and the CGA.

Where key differences between the New Zealand legislation and the overseas legislation have been identified, these are examined in more depth and the advantages and disadvantages for New Zealand of adopting such provisions are considered.

Unlike New Zealand, the other jurisdictions have consumer protection legislation at the national and the state, local or provincial level. For the purposes of this comparison exercise, the FTA and the CGA have been compared with consumer protection legislation found at both levels of government. Given the size of the New Zealand market and the fact that consumer protection is a national issue with no recognised regional differences in this country, the option of legislating for consumer protection at both the local as well as the national level was not considered as part of the analysis.

Similarities across the Jurisdictions

Overall, the FTA and the CGA contain prohibitions and redress and enforcement provisions that are very similar to those that are available in consumer protection legislation in Australia, the United Kingdom, Canada and the United States of America.

In all these jurisdictions, the legislation contains prohibitions that intervene in the market at the pre market, market and after market stages. Misleading and deceptive conduct and pyramid schemes are prohibited and all the legislation contains product safety provisions.

The legislation across the jurisdictions also usually contains redress and/or enforcement provisions. When contraventions of the guarantee (conditions and warranties) provisions occur, consumers are usually (except for in the United States) required to take action for themselves in order to get redress.

Civil and criminal penalties are available in most legislation and consumers can take disputes to a small claims or dispute tribunal as well as to courts.

Enforcement agencies are responsible for taking action under some of the legislation. As well as enforcement, these agencies often also have or adopt an educative or information provision role. In all cases, the enforcement agencies that operate at the national (or federal) level do not act on behalf of individual consumers in order to settle disputes.

The fines available in the legislation are similar across the jurisdictions with the highest fines found in the Australian legislation. As well as court proceedings, settlements and undertakings are also used by enforcement agencies in an attempt to secure compliance with the legislation.

In Summary

- New Zealand's consumer protection legislation remains consistent with consumer protection legislation in similar jurisdictions overseas.
- The overseas legislation is seeking to achieve similar outcomes to the FTA and the CGA
 - Traders comply with the legislation;
 - Consumers have effective access to redress; and
 - Consumers seek redress when a transaction is unsatisfactory.
- Whilst there are no significantly different approaches in the overseas legislation, analysis has indicated that there may be some additional, particularly mid level enforcement tools, that may be worth considering for adoption.

Differences across the Jurisdictions

The following table identifies the main differences that were found between consumer protection legislation in New Zealand, Australia, Canada, the United Kingdom and the United States of America.

Table 1: Differences across the Jurisdictions

	Jurisdiction				
Issue	NZ	Australia	Canada	UK	US
Definition of consumer	Consumer definition in the CGA focuses on consumers and type and use of goods.	Consumer definition includes consumers and small business.	Provincial definitions define consumers as non-traders.	General definitions in various statutes. Consumers are non-traders.	FTC ¹² law has several definitions of consumer, depending on context. If comparison is made with legislation that has provisions that are the equivalent of CGA, the consumer definition is very similar to NZ definition.

¹² Federal Trade Commission.

	Jurisdiction				
Issue	NZ	Australia	Canada	UK	US
Prohibitions – unfair terms in consumer contracts	No specific prohibition for unfair terms in consumer contracts.	Unfair terms in consumer contracts are prohibited in state of Victoria.	Many provincial governments prohibit unfair practices which include unfair terms in consumer contracts.	Unfair terms in consumer contracts are prohibited.	The <i>Uniform Commercial Code</i> (adopted by most states) prohibits terms in contracts that are unconscionable.
Prohibitions – unconscionable conduct	Unconscionable conduct is covered by common law and Section 19 (1) (e) and (f) of the Disputes Tribunal Act 1988. Courts must decide if conduct is unconscionable.	Unconscionable conduct is covered by statute as well as common law. Courts must decide if conduct is unconscionable.	Unconscionable conduct prohibitions are in statute.	Unconscionable conduct is covered by common law only. Courts must decide if conduct is unconscionable.	<i>Uniform Commercial Code</i> prohibits unbalanced contracts, but unconscionable conduct is left to the courts to decide.

	Jurisdiction				
Issue	NZ	Australia	Canada	UK	US
Industry codes of conduct	Provisions covering industry codes of practice are not in legislation.	Provisions covering industry codes in legislation and overseen by ACCC. ¹³	Provisions covering industry codes of practice are not in legislation.	Legislation allows the OFT ¹⁴ to approve and promote industry codes.	Provisions covering industry codes of practice are not in legislation.
Enforcement – court enforceable undertakings	No court-enforceable undertakings available. The Commerce Commission uses the administrative system of settlements.	At federal and state level, contravention of an undertaking can result in court action by the enforcement agency.	At federal and provincial level, contravention of an undertaking can result in court action by the enforcement agency.	Contravention of an undertaking can result in court action by the enforcement agency.	Breach of a “cease and desist” order (more of an undertaking) can result in court action taken by the enforcement agency and a fine.

¹³ Australian Competition and Consumer Commission.

¹⁴ Office of Fair Trading.

	Jurisdiction				
Issue	NZ	Australia	Canada	UK	US
Enforcement – compulsory Interview	No ability to require a trader to attend a compulsory interview.	ACCC has the power to issue demands for information, including appearing before the ACCC in person. Also a requirement in some state legislation.	Traders voluntarily attend an interview at both federal and provincial level.	Formal interviews can be carried out, in accordance with The Police and Criminal Evidence Act 1984.	“Civil Investigative Demands” can be used to gain verbal testimony.
Enforcement – banning traders	No ability to ban a recidivist offender.	Some states can ban traders from supplying goods and services.	Courts can ban individuals from trading for a period of time.	No banning provisions.	Courts have the ability to bar an individual from making claims without substantiation. Provisions appear to ban activities rather than individuals.

	Jurisdiction				
Issue	NZ	Australia	Canada	UK	US
Enforcement- super-complaints	Consumer bodies do not have a special ability to refer consumer complaints to Commerce Commission.	Consumer bodies do not have a special ability to refer consumer complaints to ACCC.	Consumer bodies do not have a special ability to refer consumer complaints to the enforcement agencies.	Designated consumer bodies can lodge super-complaints to the OFT.	Consumer bodies do not have a special ability to refer consumer complaints to the enforcement agencies.
Enforcement- product safety	No requirement for Product Safety Warning Notices.	Product Safety Warning Notices published in the <i>Gazette</i> announce when a good is under investigation for being unsafe.	No warning notices. Notification of warning through press releases.	No warning notices. Notification of warning through press releases.	No warning notices. Onus on companies to issue forms of notification.
Redress- defective product	A person who has suffered injury from a defective product is covered by ACC. ¹⁵	A person who has suffered loss or damage from a defective product can take private court action.	A person who has suffered loss or damage from a defective product can take private court action.	A person who has suffered loss or damage from a defective product can take private court action.	A person who has suffered loss or damage from a defective product can take private court action.

¹⁵ Accident Compensation Corporation administers New Zealand's accident compensation scheme, which provides personal injury cover for all New Zealand citizens, residents and temporary visitors to New Zealand. In return people do not have the right to sue for personal injury, other than for exemplary damages.

	Jurisdiction				
Issue	NZ	Australia	Canada	UK	US
Enforcement-substantiation Notices	No substantiation notices requiring traders to prove claims.	Substantiation notices can be issued to traders to require them to prove claims.	Competition Act requires advertisers to substantiate all material claims.	Advertisers are required to provide substantiation for claims to UK ASA ¹⁶ if a complaint is received.	FTC has a substantiation policy for advertising.
Enforcement-cease and desist	No cease and desist orders.	No cease and desist orders at federal level but available in some states.	Cease and desist orders available.	Enforcement orders under the Enterprise Act.	Cease and desist orders under the FTCA. Cease and desist orders are assessed by a district court.

¹⁶ United Kingdom Advertising Standards Authority.

	Jurisdiction				
Issue	NZ	Australia	Canada	UK	US
Enforcement-penalties – formal cautions	No formal cautions.	No formal cautions.	No formal cautions.	Formal cautions provide an alternative to prosecution and are recorded on the Central Register of Convictions.	No formal cautions.

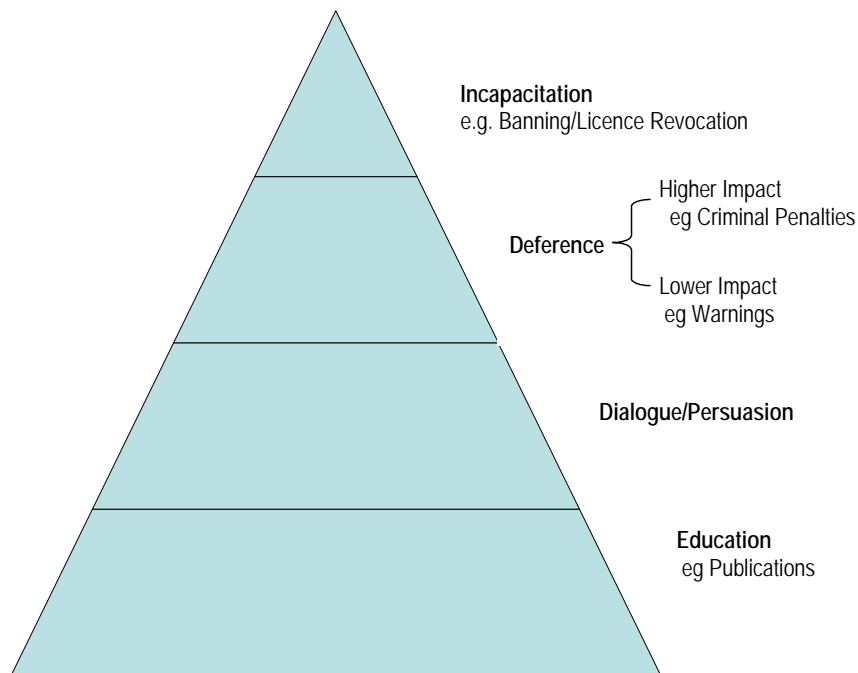
The Pyramid of Responsive Regulation

The comparison shows that, compared to overseas regulation, New Zealand consumer protection law is limited in the range of sanctions (particularly mid-level) that it can use in an attempt to secure compliance with the FTA.

Regulatory compliance is best secured when enforcement agencies use persuasion and negotiation techniques rather than enforcement measures. For these techniques to be effective, however, enforcement agencies must have at their disposal a range of escalating sanctions which can be used if an individual or business chooses not to cooperate or when the contravention represents a serious breach of the legislation. Non-compliance is less attractive for individuals and businesses if the enforcement agency is able to escalate the sanction should persuasion be ineffective or inappropriate given the nature of the alleged breach.

The process whereby enforcement agencies can escalate the level of sanctions that they use is often depicted by way of the pyramid of responsive regulation. At the base of the pyramid are the most frequently used and least severe sanctions while the most severe sanctions are found at the peak. According to this model, enforcement agencies that have a number of sanctions at their disposal, as depicted by a tall pyramid, are the most effective. This is because the sanctions at the peak can exert pressure which can motivate individuals and businesses to voluntarily comply – the threat of a more severe form of punishment encourages individuals and businesses to comply.

Figure 1: Pyramid of Responsive Regulation



(Adapted from the work of Ayres and Braithwaite (1992) and Gilligan, Bird and Ramsay, 1999)

Compared with the range of sanctions available in similar legislation overseas, New Zealand's FTA lacks a number of sanctions particularly those that are represented in the mid levels of the pyramid of responsive regulation. The FTA provides for civil and criminal remedies. The Commerce Commission has also developed an administrative system whereby it issues letters of compliance, warnings and enters into settlements with parties. Unlike enforcement agencies in other jurisdictions, the Commerce Commission cannot issue product safety warning notices or cease and desist orders, require businesses to substantiate claims and accept court enforceable undertakings or require individuals to attend a compulsory interview. If the Commission believes that an alleged breach of the Act has occurred that can not be adequately dealt with administratively, the only alternative is to take court action. Court action, however, is resource intensive and the presence of mid-level enforcement sanctions mean that the same outcome could be achieved more efficiently. In the last three years, according to the Commerce Commission, the costs of litigation have trebled and the number of Fair Trading Act cases in the court system has doubled.

As well as lacking the mid level enforcement sanctions, the FTA does not contain penalties that can incapacitate recidivist offenders.¹⁷ In other jurisdictions, enforcement agencies have the ability to apply for incapacitative orders which can prevent an individual from trading. The severest sanctions available under the Fair Trading Act are civil and criminal penalties. These penalties take the form of monetary fines. The maximum fines available are \$60,000 for an individual and \$200,000¹⁸ for a body corporate. Monetary penalties, however, do not appear to act as a deterrent when used against recidivist offenders. In 1994, for example, the Commerce Commission obtained interim injunctions against Michael Knight relating to alleged breaches of the FTA by two companies that he had promoted. Knight then transferred his business activities to Australia where he was subsequently banned for life from trading in New South Wales and restrained from engaging in trade or commerce relating to the tourism industry in Queensland. Following his return to New Zealand, Knight was convicted in April 2002 of thirty three breaches of the FTA. Knight was also sentenced in July 2004 on 12 further charges of breaching the Fair Trading Act.

¹⁷ Incapacitative sanctions are found at the apex of the pyramid of responsive regulation.

¹⁸ If a person is convicted of promoting or operating a pyramid selling scheme (section 24 of the FTA) they are liable on summary conviction to a fine not exceeding \$200,000. On application by the Commerce Commission, the court may also order a person to pay an amount not exceeding the value of any commercial gain resulting from the contravention.

Part 3 – Legislative Differences Proposed for Adoption

This part of the discussion paper identifies prohibitions, investigation and enforcement tools and penalties that are found in the consumer protection legislation in the other jurisdictions but are not currently available in the Fair Trading Act. It is considered that these amendments would strengthen the Fair Trading Act in terms of achieving the desired outcomes for consumers and businesses.

The tools that have been analysed are –

- Unfair terms in consumer contracts prohibition;
- Product safety warning notice and powers of investigation;
- Cease and desist orders;
- Substantiation notices;
- Court enforceable undertakings;
- Compulsory interview;
- Banning orders.

Some of the proposals, (for example, the those relating to compulsory interviews, the ability to make cease and desist orders and obtain court enforceable undertakings) could assist the Commerce Commission in its enforcement role by enabling it to act more quickly when it believes that a contravention has occurred. Enabling the Commerce Commission to act in this way could reduce the amount of consumer detriment that can result from contraventions of the Fair Trading Act. Some of the tools can be used together to improve the enforcement outcomes for both compliant businesses and consumers. Including these redress and enforcement provisions in the Fair Trading Act should provide better protection for consumers and thereby allow them to transact with more confidence.

The following analysis tests thinking in the area of the enforcement of consumer protection law and MCA is interested to hear your views on the proposals.

Unfair Terms in Consumer Contracts Prohibition

Issue

An unfair term in a contract is one that causes a party (usually the consumer) to be at a disadvantage while the term is not reasonably necessary for the protection of the interests of the other party (usually a business). Typically, an unfair term is a pre-written standard term. A standard term is a term created by the business in advance of a contractual agreement and is not negotiated separately with each consumer. A negotiated term is agreed upon by both the business and each individual consumer. Unfair terms have been defined in other jurisdictions as contrary to the requirement

of good faith that cause a significant imbalance in the parties' rights and obligations under the contract to the detriment of consumers. A term that states that a trader may change or alter other terms in a contract without consulting the consumer is an example of an unfair term.

Under Part 1 of the Fair Trading Act (FTA), misleading and deceptive conduct, false representations and unfair practices are prohibited. Unfair terms in contracts are not specifically prohibited. They are covered under general contract law¹⁹ and common law.²⁰ However, it is uncommon for consumers to take court action under these for unfair terms.

In many instances, consumers do not realise that a term is unfair, or that the term can be negotiated, especially if it is pre-written into the contract. The consequence of a consumer agreeing to a contract with such terms is that they may find themselves bearing most of the cost and/or risk of the transaction. For example, Consumer Affairs Victoria (Australia) notes an example of an unfair term in car rental agreements, where the consumer is required to acknowledge the car is in good condition, clean and roadworthy. While the consumer can see the car is clean, they cannot know the mechanical condition or safety (roadworthiness) of the vehicle.²¹

Consumers may also find they do not have fair and reasonable access to a variety of goods and services in the marketplace. Unfair terms may bind the consumer into a contract where they cannot use other businesses. For example, a contract may bind the consumer to the terms and conditions of the supplier's insurance scheme that the consumer has not looked into and is therefore denied the choice of using another insurer.

The Ministry of Consumer Affairs and the Commerce Commission have received complaints from consumers where the terms in contracts may not be misleading or deceptive but they do appear to be unfair. Even when consumers recognise that the terms are unfair they sometimes feel they have little option but to sign as there is little or no difference in the contracts used by all providers in that sector.

International Comparisons

In several of the other jurisdictions analysed for comparison with New Zealand, consumer protection legislation specifically prohibits unfair terms. When the enforcement agencies believe that a contract term is unfair they can take enforcement action even when consumers have signed a contract.

¹⁹ For example, the Contract Remedies Act 1979

²⁰ The common-law legal system forms a major part of the law of many countries, especially those with a history as British territories or colonies. It is the unwritten law purporting to be derived from ancient usage and judges decisions (Oxford English Dictionary).

²¹ Consumer Affairs Victoria [www.consumer.vic.gov.au]. *Fair Trading: Unfair Terms in Vehicle Rental Agreements 2005*, Melbourne, Australia.

In the United Kingdom, the Unfair Terms in Consumer Contracts Regulations 1999 state that a consumer is not bound by any standard term in a contract that is unfair.²²

The Unfair Terms in Consumer Contracts Regulations 1999²³ provide, in a schedule to the Regulations, an indicative but non-exhaustive list of unfair terms. If the Office of Fair Trading (OFT)²⁴ suspects that a term is unfair, then it can investigate and may take court action. The court may issue an injunction to stop a trader using the unfair term.

The Fair Trading Act 1999²⁵ in Victoria, Australia also legislates against unfair terms. The provisions found in the Act are based on the United Kingdom Regulations (outlined above). Under Victoria's legislation, consumers can take civil action²⁶ against a supplier to have an unfair term declared void. Consumer Affairs Victoria (CAV) can also apply for an injunction to stop a trader using an unfair term. Penalties for the use of unfair contract terms are A\$1,000 for individuals and A\$2,000 for corporations. CAV also works with targeted industry groups to develop fair standard terms in their consumer contracts. To date CAV has worked with the mobile phone, hire car and fitness centre industries. The priority areas for the 2005/2006 year are pay television, internet service providers, home removalists and building contracts.

Comparing the regimes, the Unfair Terms in Consumer Contracts Regulations in the United Kingdom apply to standard contract terms, while in the Victorian Fair Trading Act the unfair term provisions may apply to both standard and negotiated terms. The term "unfair" is defined in a general way in both pieces of legislation and a non-exhaustive list of what may constitute an unfair term is provided. In both the United Kingdom and in the state of Victoria only a court²⁷ can decide whether a term is

²² A seller or supplier is also required to ensure that any written term of a contract is expressed in plain, intelligible language.

²³ Unfair Terms in Consumer Contracts Regulations 1999 [link to OPSI website] [www.opsi.gov.uk/si/si1999/19992083.htm].

²⁴ Under the Unfair Terms in Consumer Contracts Regulations, the OFT has a duty to consider any complaints that it receives about unfair contract terms. Other organisations listed in Schedule 1 as qualifying bodies can also investigate unfair terms.

²⁵ Fair Trading Act 1999 [link to Victorian Legislation and Parliamentary Documents website] [www.dms.dpc.vic.gov.au].

²⁶ In determining whether a term is unfair, a court or the Victorian Civil and Administrative Tribunal (VCAT) may take it into account whether a term was individually negotiated if such a determination does not limit the unfair term definition. VCAT deals with disputes about:

- purchase and supply of goods and services
- discrimination
- domestic building works
- guardianship and administration
- residential and retail tenancies
- consumer credit.

²⁷ This includes VCAT.

unfair. If court action is successful, the injunction usually covers only the unfair term. It is less usual for the entire contract to be declared void.

The OFT has a duty to consider every complaint that it receives about an unfair contract term. CAV is not constrained in this way and has taken a proactive approach in dealing with the issue of unfair terms in contracts. Rather than solely relying on consumers recognising unfair terms in contracts and taking a dispute to the Victorian Civil and Administrative Tribunal or making a complaint, CAV has identified specific industry groups that use standard contract terms and has worked with them to develop contracts that in the opinion of the CAV do not breach their Fair Trading Act. While such an approach can have the effect of changing a number of contracts that are commonly entered into by consumers, it can also be resource intensive.

Although other Australian states do not currently have specific legislation prohibiting unfair terms, they have made a commitment to promote amendments to their consumer legislation that may prohibit unfair terms.

Internationally, some telecommunications companies have required in their contracts that customers pay for all calls made from their telephones irrespective of whether they authorised the call. In some jurisdictions this contract term has been ruled unfair.

Discussion

Specifically prohibiting unfair terms in consumer contracts in the FTA, even if they are not misleading or deceptive, would enable the Commerce Commission to take enforcement action against businesses using unfair terms in their consumer contracts. As well, if unfair terms were prohibited, individual consumers would be able to take a dispute about an unfair term in a contract to the Disputes Tribunal (or even to court) on their own behalf.

Currently unfair terms are not defined in the FTA. It is suggested that any amendment prohibiting such terms should follow the approach taken in the United Kingdom and Australia in providing an indicative non-exhaustive list to aid decisions by the court. As noted, in the United Kingdom the OFT is required to investigate every unfair term complaint. It is not proposed that a similar approach be taken in New Zealand. Rather, it would be up to the Commerce Commission to decide how to enforce any breach.

A prohibition of unfair terms would provide an opportunity for the Commission to work with industry groups (in an educative way) to develop fair standard terms. This approach can resolve issues in a pro-active and co-operative manner and may prevent court action being taken.

Prohibiting unfair terms would thus expand on the current suite of prohibitions including misleading or deceptive conduct, false representations and unfair practices, and this should allow consumers to enter into contracts with greater confidence.

Proposal

MCA considers that there is merit in proposing that the Fair Trading Act be amended so that it contains provisions where unfair contract terms are specifically prohibited.

Product Safety Warning Notice and Powers of Investigation

Issue

The present Fair Trading Act (FTA) investigative powers (search and seizure) for product safety enforcement are limited to investigating and enforcing compliance with existing product specific measures (safety standards, bans and compulsory recalls). When a safety problem is recognised during the investigative stage, there are no powers to remove the product from sale, exposing consumers to potential harm.

There are also no formal powers by which the Minister or relevant officials can warn the public of the possible harm that may be caused by the products under investigation.

Accordingly, product safety redress and enforcement in the initial investigation stages relies mainly on the goodwill of businesses to stop selling products identified as unsafe. If this fails, action can be undertaken by the Minister of Consumer Affairs. This takes the form of Unsafe Goods Notices, where products classified as unsafe are required to be removed from the market, or compulsory recalls, where the Minister requires the trader to recall the product. Unsafe products may then be the subject of a Product Safety Standard, which outline construction, composition, testing and warnings that apply in respect of a particular product, for example the distance between vertical bars in a cot to prevent a baby's head from getting wedged.

Investigations and the development of Unsafe Goods Notices and compulsory recall orders are actioned by officers of the Ministry of Consumer Affairs (MCA) who have no powers of search and seizure. The Commerce Commission officers can enter premises and seize product but only after an Unsafe Goods Notice or compulsory recall order has been issued, or where a product subject to a product safety standard is believed to be in breach of a standard.

There is a concern that the FTA powers are not sufficient in that they do not allow for the very quick removal of product from sale when potential safety problems are recognised during the investigative stage, exposing consumers to potential harm.

International Comparisons

Product safety is managed in various ways in the consumer protection legislation in the other jurisdictions analysed for comparison. In Canada, Health Canada takes the lead in controlling and enforcing product safety of all types. In the United States, the Consumer Product Safety Commission has prime responsibility for the 15 000 consumer products within its jurisdiction. Both of these organisations develop voluntary standards, issue and enforce mandatory standards, ban products when no standards would adequately protect consumers, undertake recalls, research potential product hazards and educate consumers.

In the United Kingdom, the General Product Safety Regulations 2005 have introduced an obligation on businesses to only place safe product on the market. The Regulations also require businesses to provide consumers with relevant information to assist them in assessing the risks of using the product, and manufacturers must adopt measures so that they are informed of risks and can take action if necessary. Some offences are criminal and some are civil.

The New Zealand FTA product safety provisions are similar to those found in the Australian Trade Practices Act (TPA). There are, however, two main differences in that the TPA provides for:

- Warning notices; and
- Powers of investigation.

The TPA at section 65B includes provisions for issuing warning notices to the public, where the Minister may publish in the Gazette a notice outlining when a good is under investigation in order to determine whether it will or may cause injury and/or the possible risks involved in the use of the specified good. These provisions were included in the TPA very soon after New Zealand's FTA was passed into law.

As well, the Australian Competition and Consumer Commission (ACCC) can seize products that are under investigation. The ACCC is responsible for implementation of the TPA, including product safety. The Australian states have included the product safety provisions of the TPA into their own consumer protection legislation but also have the ability to differ in their enforcement regimes. For example, a temporary ban can be imposed for between 28 days and 18 months depending on the state. In Tasmania, the ban can be indefinite.

Australia is currently reviewing its product safety regime. A report by the Australian Productivity Commission was released on 7 February 2006. Several options have been proposed, including a general product safety provision like that in the United Kingdom. The Australian review will have an impact on product safety in this country as many New Zealand manufacturers trade in Australia under the Closer Economic Relations (CER) agreement and the Trans Tasman Mutual Recognition Arrangement (TTMRA) which provides that goods legally sold in one country may be legally sold in the other. It is not clear at this stage whether Australia will amend its product safety requirements.

Discussion

Search and seizure powers of a similar nature to those in the TPA in Australia could help to achieve a more effective product safety system in New Zealand. The ability to remove potentially unsafe product from the market more quickly could help to reduce consumer exposure to products that could cause harm.

If a product is subsequently found to be safe, the product can be returned to the trader and be returned to the market. Likewise if a product can be made safe by applying conditions relating to, for example, its composition by way of a product safety standard, the product could be returned to the market by way of the existing Product Safety Standards mechanism.

It is also proposed that the Minister of Consumer Affairs have the power to delegate to either MCA or Commerce Commission officers (as appropriate) the power to seize product pending the outcome of an investigation. In the United Kingdom, Canada and the United States such powers are held at the investigating officer level.

Although under the TPA the ACCC has the ability to issue a warning about a product, it appears that most businesses voluntarily comply with the ACCC on product safety issues. The ability to warn the public may be encouraging the traders to comply.

Being able to warn the public that a product is under investigation when a trader refuses to comply voluntarily reduces the chance that harm may occur to consumers. Consumers are then given the opportunity to stop using, or to modify the way they use the product.

Adding search and seizure and warning notice powers to the FTA also continues the similar nature of New Zealand and Australia product safety legislation.

Proposal

MCA considers that there is merit in providing in the Fair Trading Act:

- the power for the Minister of Consumer Affairs to authorise persons (exercised under warrant) to seize potentially unsafe products during investigations into that product's safety; and
- the power for the Minister to issue warnings to the public regarding potentially unsafe products that are the subject of an investigation.

If a decision is made to progress with this proposal, the Ministry of Consumer Affairs will have to give further consideration to the practical implications of implementing of such a provision including an appropriate threshold for the seizure of potentially unsafe products.

Cease and Desist Orders

Issue

Cease and desist orders are formal administrative injunctions that require traders/businesses to cease conduct that allegedly breaches the Act.

Breaches of the Fair Trading Act (FTA) can cause considerable detriment to consumers. Currently, the FTA does not have cease and desist provisions, so when the Commerce Commission believes that there is a breach of the Act it cannot force a trader to cease the conduct until it has taken court proceedings. This means that while breaches are being investigated and during the court process, businesses may continue to engage in conduct which may cause considerable harm to consumers. If the Commission had the power to issue a cease and desist order, it could very quickly prevent a trader continuing with the alleged misconduct.

In September 2001, the Commission commenced a prosecution against a trader which related to claimed nutritional benefits of taking a product marketed by the

company. There were a number of lengthy delays in hearing the case, primarily resulting from the availability of expert witnesses. The defended hearing finally took place in April to June 2004 and judgment not received until June 2005 when the company was convicted of the charges. During the period of nearly four years until the judgment was made, the company continued to promote the product using many of the representations that were later found by the court to be in breach of the Fair Trading Act.

Under the Commerce Act 1986, the Commerce Commission can make a cease and desist order where there is a prima facie case that a person has engaged in a restrictive trade practice (section 80 (1)) or has contravened the business acquisition provisions (section 83(1)) and it is necessary for the Commission to act urgently. A cease and desist order prevents a person from engaging in conduct as identified in the order.

The Commerce Act's cease and desist order process involves an investigation of the breach by the Commission, then a referral to a Cease and Desist Commissioner who decides whether or not the conduct contravenes the Act. The person who is the subject of the order is consulted and can consent to the terms of the proposed order or can decide to have the matter determined by the Commissioner following a hearing.

A cease and desist order can be made if the Cease and Desist Commissioner is satisfied that a case has been made and it is necessary to act urgently to prevent consumers from suffering serious loss or damage and/or harm in the interests of the public. Failure to comply with an order would result in an application for a penalty to the High Court.

A cease and desist order is deemed to be a Commerce Commission decision and is subject to appeal in accordance with sections 91-97 of the Commerce Act.

International Comparisons

In the United States and Canada,²⁸ cease and desist orders are available in their consumer protection legislation. These are administrative rather than judicial orders. Court action is not required before they are issued. Their advantage is that the level of proof required is not as high as that needed for an injunction.

In the United States, the Federal Trade Commission can issue cease and desist orders if there is reason to believe that the Federal Trade Commission Act has been breached. The process is complex, with the trader allowed several opportunities to appeal. The final order is binding 60 days after its issue.

Canada has a form of cease and desist order, where the Competition Commissioner can make an application for an interim order lasting up to 10 days. The trader is

²⁸ In the United Kingdom, the Enterprise Act 2002 has Enforcement Orders. These are essentially injunctions rather than cease and desist orders but may only be taken where the breach may harm (or potentially harm) the collective interests of consumers. They cannot be used for consumers seeking individual redress.

given 48 hours notice prior to the issuing of the order. The period the order covers can be extended to allow for the Commissioner to undertake an investigation. An interim order can only be granted under serious circumstances, and it is understood that the Competition Tribunal has never used this power. The Competition Commissioner can also apply for interim and permanent injunctions, which appear to be the preferred enforcement tool.

The Australian Trade Practices Act (TPA) does not provide for cease and desist orders for either competition or consumer law. In a review of the TPA by the Australian Treasury in 2003, competition cease and desist orders internationally were discussed and analysed. The Australian Treasury concluded that there was little evidence that cease and desist orders were faster, cheaper or more effective than injunctions with respect to breaches of competition law and saw little need for an additional process. There appears, however, to have been no analysis with regard to consumer protection law breaches.

Discussion

Amending the FTA so that the Commerce Commission can make cease and desist orders would mean that behaviour that contravenes the legislation could be stopped more quickly than presently occurs following court proceedings.

This is important because the costs and delays associated with FTA litigation have increased significantly during the last three years. In that time, according to the Commerce Commission, the costs of litigation have trebled and the number of FTA cases in the court system has doubled.

The Commerce Commission has not used the cease and desist provisions under the Commerce Act since they came into force on 1 April 2002. They are, however, considered by the Commission to be a useful enforcement option, which may be better suited to consumer protection issues than to competition issues. This is because it is often easier to demonstrate a breach and also to demonstrate that consumers are suffering serious loss or damage as a result.

Injunctions can be used to stop businesses from behaving in a manner that contravenes the legislation. Under the FTA, injunctions may be granted by the court for contraventions of parts I, II, III and IV of the Act. The test that is used for the granting of an injunction, however, is very different from that which would apply at a cease and desist hearing. A cease and desist commissioner is required to make decisions on the basis of whether there is a prima facie breach of the Act and the detriment to consumers.

Injunctions are granted on the basis of the balance of convenience test. Under this test an assessment is made as to what would happen if an injunction was made and the interests of the trader (including commercial loss) are balanced against those of consumers. The balance of convenience test will typically tip in favour of businesses unless it is proven that consumers have suffered a significant detriment, for example, lost their life savings. Therefore injunctions are not necessarily the best option for consumer protection.

In 1999, the Commerce Commission sought an injunction against Alpha Club New Zealand Limited alleging breaches of section 24 of the Fair Trading Act (operating a pyramid selling scheme) and section 9 (misleading and deceptive conduct). The Commission wanted to prevent Alpha from continuing to operate in New Zealand, recruiting new members (who were likely to lose money), and preventing the dissipation of funds accumulated by the company as profit. The judge considered the balance of convenience test and concluded that, as the result of such an injunction, the business would close down and this consequence outweighed the detriment to existing (and future) members of Alpha Club and the wider public. The injunction was not granted, although 26% of the business profits were ordered to be set aside. The matter was then taken to the High Court and, in 2002, judgment was found in favour of the Commission. The Commission was instructed that the money set aside as a result of the failed injunction was to be returned to those people who had joined Alpha Club after December 1999. However, only a partial membership list was available, so the Commission had to advertise and locate the remaining members of the Club. The judge ordered the cost of finding members to be taken out of the retained funds and that any remaining money be distributed on a pro-rata basis to the members.

In comparison with the court process, cease and desist orders are low cost, can be introduced quickly, and prevent continuing cost to the economy, consumers and compliant businesses.

Proposal

MCA considers that there is merit in proposing that the Fair Trading Act be amended so that the Commerce Commission can make cease and desist orders.

Substantiation Notices

Issue

Under the Fair Trading Act (FTA) misleading or deceptive representations are prohibited.

There are, however, no statutory powers in the Fair Trading Act to allow the Commerce Commission to require, by way of issuing notices, substantiation of claims or representations from businesses, which means that the onus of proof usually falls on the Commission to demonstrate that a claim cannot be substantiated.

This can be particularly difficult for the Commission where the claims relate to comparative pricing issues or technical or scientific declarations. In such instances the Commission usually has to go to considerable expense and often has to employ significant resources in order to prove that such a claim cannot be substantiated. Gathering good evidence to prove a claim cannot be substantiated can also be time consuming, leaving consumers exposed to potentially misleading or deceptive representations for some time.

In a case recently prosecuted by the Commerce Commission a trader promoted a slimming product. False or misleading claims were made that it would melt away cellulite and fat and that it had been tested and approved by experts in Europe and

America. Part way through the period during which the trader was vigorously marketing the product, he was warned by another agency that its promotion was likely to be illegal. When approached by Commission staff, the trader acknowledged that he had copied marketing material received from overseas as a direct mail letter and was not able to substantiate the claims made. The trader had also taken no steps to have the product tested or to verify the representations made about the product in the promotional material.

Around 1,250 customers purchased the product paying approximately \$176,000 in total. When the case eventually came before the court, the trader pleaded guilty to a number of breaches of the Fair Trading Act, although an appeal against the level of penalty and compensation orders has yet to be heard. In order to bring the case, the Commission paid nearly \$40,000 on the necessary expert evidence required for a successful court case. That sum would have been significantly higher had the trader not pleaded guilty. The sentencing was decided in November 2005, over three years after the trader's distribution of the product had ceased, during which time the affected consumers have had to wait to receive any compensation.

Complaints relating to claims made in advertisements can be dealt with by the Advertising Standards Authority (ASA) which can request evidence to support a claim made. This process only covers advertising claims. It does not cover labelling or packaging claims, unless they can be seen in an advertisement.

International Comparisons

In several states in Australia, the consumer protection legislation provides for substantiation notices. These notices require a business to substantiate the expressed or implied claims made in advertisements or on labels or packages, and in the case of New South Wales, also extends to requiring real estate agents to substantiate selling price estimates.

If a substantiation notice is served on a business it is required to provide evidence, demonstrating that a claim can be substantiated, to the Director-General of Fair Trading (or other equivalent person) within the time specified by the notice. It is an offence not to comply with the notice or to knowingly provide information that is false or misleading. It is also an offence for a business to be unable to substantiate a claim made in the marketplace.

Based on the business's response, the regulator assesses what action should be taken. If the business cannot substantiate the claims, it is often required to give an undertaking that it will cease making such claims. A consumer cannot seek damages because a business fails to substantiate their claims. Instead, the consumer can claim damages leading from any misleading and deceptive conduct.

The United States Federal Trade Commission (FTC) has an advertising substantiation policy which states that by making claims, an advertiser is indicating it has supporting evidence for those claims. A trader's failure to support its claims constitutes an unfair and deceptive act or practice in violation of section 5 of the Federal Trade Commission Act. The FTC can also use its cease and desist orders to require a trader to:

- stop running the deceptive advertisement or engaging in the deceptive practice,
- substantiate claims in future advertisement; and
- report to FTC staff about the substantiation it has for claims in new advertisements.

Violations of cease and desist orders can result in civil penalties of up to US\$11,000 per violation.

In the United Kingdom the Control of Misleading Advertisements Regulations 1988 implements a European Community Directive on misleading advertising. The Regulations aim to protect the interests of consumers and businesses from misleading advertising – or advertisements that make prohibited comparisons. Most complaints about misleading non-broadcast advertisements are handled by the United Kingdom Advertising Standards Authority (United Kingdom ASA) and the Trading Standards Service. If an advertisement is found to break the British Codes of Advertising and Sales Promotion, the United Kingdom ASA will ask the company to withdraw or change the advertisement. Advertisers are required to prove that any claims they make are capable of objective substantiation. The codes, devised by the Committee of Advertising Practice, cover most forms of non-broadcast advertising.

Canada has a comprehensive regulatory regime that deals with unsubstantiated claims. The Competition Act requires advertisers to substantiate all of their material²⁹ claims. Guarantees, efficacy, lifespan and other statements must be based on adequate and proper tests. While these tests are flexible to accommodate the vast variety of claims, guidelines and industry codes help to remove uncertainty about the appropriate tests and how to apply them. If claims are not based on adequate and proper tests, they then become “reviewable conduct”. This means the conduct can be investigated by the Competition Bureau. It is a criminal offence if the misrepresentation is shown to be made knowingly or recklessly and the following sanctions can be imposed:

- a cease and desist order for up to 10 years;
- a requirement that the advertiser publish a notice of the misleading claim and the court’s order;
- CAD\$50,000 (first order) or CAD\$100,000 (subsequent orders) for an individual, and CAD\$100,000 (first order) or CAD\$200,000 (subsequent orders) for a corporation.

If the Competition Bureau takes a case to court, the directors and officers of the advertiser can face up to five years imprisonment and a court imposed fine.

²⁹ "Material" means important or essential in this context.

Discussion

As indicated above, substantiation notices are an accepted consumer policy enforcement tool in all of the international comparison jurisdictions. They also place the onus of proof of claims on the trader, not the enforcement agency. Currently, the Commerce Commission is required to prove that claims cannot be substantiated. Such investigations can be very resource intensive. A recent comparative pricing investigation, for example, has involved around 80 covert store visits by Commission investigators. It is likely that such labour intensive investigations generally could be avoided if the Commission was able to require businesses to substantiate their claims (refer also to the example highlighted above).

The costs to the Commission of proving that a product's claim is unsubstantiated can be very high. In a recent case, for example, the cost to the Commission was \$177,897 for expert and legal expenses. This figure covers external costs only and does not include the Commission's internal legal and investigative expenses.

If the FTA was amended to enable the issuing of substantiation notices, any person who received a substantiation notice would be required to support the claims that they make about their products or services. The Commission would then be able to assess the validity of the information supporting the claim and base any action on the basis of that response. Where there is inadequate information, or no information is supplied, the Commerce Commission would be likely to take a case against the business on the basis that they are allegedly making false and misleading representations.

For a substantiation notice provision to be effective, a trader would not be able to refuse to provide evidence, be able to ignore a notice or to knowingly provide information that is false or misleading without committing an offence.

It is not expected that the ASA's substantiation process would be affected by amending the FTA so that the Commerce Commission could issue substantiation notices. The Commission only initiates an investigation if the issue meets its enforcement criteria. The advertising complaints process is well established and it is expected that most advertising complaints would still be directed to the ASA.³⁰

The ability of the Commerce Commission to issue substantiation notices should also encourage consumers to have greater confidence in the claims that are made about products or services.

Proposal

MCA considers that there is merit in amending the Fair Trading Act so that the Commerce Commission may require a trader to substantiate any claim that they make about a product or service.

³⁰ In 2005, 17% of advertising complaints/challenges to the ASA required the advertiser to provide substantiation to the Board. About 65% of those complaints/challenges were upheld/settled by the Board.

Court Enforceable Undertakings

Issue

Court enforceable undertakings are agreements between the enforcement agency and a business which are provided for in the consumer protection legislation. The enforcement agency can take the trader to court if the agreement is breached. Undertakings are voluntary. If a trader does not agree to an undertaking, the matter may proceed to court. The Fair Trading Act does not currently provide for court enforceable undertakings.

Currently, the Commerce Commission sometimes uses agreements known as settlements, when a business voluntarily admits that it has breached the Fair Trading Act and gives an undertaking to amend its behaviour. Settlements provide a business with the opportunity to rectify a contravention of the legislation without being prosecuted.

If a business does not comply with the agreed terms of the settlement, the Commerce Commission can initiate court proceedings for the original offences. A problem is that such action is subject to the limitation period set out in section 40(3) of the Fair Trading Act (3 years) or in the Limitation Act 1950 for civil proceedings.

Injunctions can be sought and granted against businesses for conduct that contravenes the legislation. They cannot, however, be used when a business breaches an agreement with the Commerce Commission to cease such conduct.

International Comparisons

Other jurisdictions, such as Australia, have court enforceable undertakings. Section 87B of the Australian Trade Practices Act allows the ACCC to take civil legal action against any business which has breached a term(s) of an undertaking. If the court is satisfied that a term of the undertaking has been breached, it can make civil orders including directing the business:

- To comply with the term of the undertaking, or
- To pay the amount of any financial benefit obtained as a result of the breach of undertaking, or
- To pay compensation.

Court enforceable undertakings are used by the ACCC on a regular basis.

At the state level, Queensland, the Australian Capital Territory, New South Wales, Western Australia, Victoria and the Northern Territory all allow their consumer affairs agencies to apply to a court for orders to direct a person to comply with an undertaking.

Discussion

Settlements are a cost-effective way of achieving good consumer outcomes and supporting a level playing field for business. The Commerce Commission's inability to hold businesses accountable for their part of a settlement weakens this tool. Court enforceable undertakings would seem to be a way of addressing this weakness.

As with settlements, court enforceable undertakings provide businesses with an opportunity to rectify their behaviour without being prosecuted. Undertakings are flexible in that they can be customised to different situations and can impose particular conditions upon a business. Any breach of an undertaking is an offence and can be prosecuted in court.

A property development company was offering to consumers a home ownership scheme. In fact, what was being offered to buyers was a type of rent-to-buy scheme where the title of the property would not be transferred to the purchasers until the end of the 30 year contract. If the purchasers failed to complete the 30 year contract, including making all scheduled payments, they stood to lose much of the equity which they had invested in the property. About 60 consumers appear to have bought into this scheme. In this case, the position of the home purchasers is of importance to the resolution of this matter. If successful court action is taken, complex and difficult issues of compensation will arise and the resolution process may well be lengthy. If the option of settlement with an agreement by the company to provide appropriate compensation is pursued, then this may well provide a quicker and more effective solution to the difficult compensation issues. Under current law, if the company later fails to adhere to any compensation agreement, the Commission's only recourse would be to take court action for the original offences. In a case such as this, action may not be possible as it would probably be time barred at that point.

Court enforceable undertakings are available in other New Zealand legislation. The Securities Commission, for example, has the power to accept undertakings that are enforceable in a court and this is proving to be an effective enforcement tool. An enforceable undertaking is accepted by the Securities Commission when it considers that this approach will provide the most suitable outcome. Accepting an undertaking does not prevent the Securities Commission from exercising any of its other enforcement powers if necessary.

The new anti-spam legislation, the Unsolicited Electronic Messages Bill, has also adopted court enforceable undertakings as an enforcement tool.

Court enforceable undertakings appear to be a flexible and powerful enforcement tool that has worked well for other agencies. The Commerce Commission has indicated that it would use this type of undertaking frequently.

Proposal

MCA considers that there is merit in amending the Fair Trading Act so that the Commerce Commission may use court enforceable undertakings.

Compulsory Interview

Issue

When the Commerce Commission is investigating a possible contravention of the Fair Trading Act (FTA) it can require a person, by notice, to supply information or documents. Persons required to supply information or documents have the same privileges in relation to the supply of the information and documents as witnesses have in any court. It is an offence not to comply with a notice and any person who fails to comply is liable on summary conviction to a fine not exceeding \$10,000 in the case of an individual or \$30,000 in the case of a body corporate.

While requiring a person to supply information or documents can assist the Commerce Commission in its investigations of possible contraventions of the FTA, some of the value of this provision is lost because currently the Commission cannot require a person to explain the contents of documents or information prior to any court case.

The ability to require a person to answer questions can be a valuable investigative tool. It not only allows the Commerce Commission to obtain information but also enables individuals to answer questions safe in the knowledge that they cannot incriminate themselves.

A company being investigated for a breach of the Fair Trading Act had a policy whereby no interviews were allowed with anyone apart from the Head of Finance and Administration. Instructions were issued that all contact with the Commerce Commission was to be through Head Office. In this case, the alleged misrepresentations were made by sales staff at branch level. Promises of information from branch level staff by the Head Office were not forthcoming. Not having direct contact with those personnel hindered the investigation and meant not being able to gather the best evidence.

International Comparisons

Consumer protection legislation in other jurisdictions requires persons to give evidence. Under the Australian Trade Practices Act (and certain state legislation, for example, New South Wales, Northern Territory, Victoria and South Australia), individuals can be required to appear before the Australian Competition and Consumer Commission (or the state enforcement agency).

Discussion

The Commerce Commission estimates that if it had the power to require a person to attend an interview to answer questions under the FTA it would use the power in up to 50% of its complex investigations. At present, if the Commerce Commission cannot get the information it needs by requiring persons to supply documents or information, the only other tool that it has available is a search warrant. In most cases a compulsory interview power is likely to be less intrusive than a search warrant and may be more useful in providing evidence of an offence particularly in instances where there is little written evidence of offending. It is also likely that the availability of

this power in the FTA would greatly reduce the time needed by the Commerce Commission to investigate complex cases.

Under the Commerce Act 1986 and the Credit Contracts and Consumer Finance Act 2005 (CCCFA), as well as requiring an individual to supply information or documents, the Commission can also require a person to appear before it to give evidence. Evidence that is obtained as a result of using these powers cannot be used against that person in court proceedings. The compulsory interview provision can also be found in the Securities Act.

It is an offence under the CCCFA and the Commerce Act (section 103) not to appear or to deceive or knowingly mislead the Commission. The same offence provision would seem to be appropriate in the FTA if it is amended so that a person is required to appear before the Commission and give evidence. Without the offence provision, the Commission could not require a person to comply.

Replication in the FTA of the provisions in the Commerce Act and the CCCFA relating to the requirement to give evidence would need to consider appropriate immunity provisions. The immunity provisions in the Commerce Act and CCCFA give a person required to appear before the Commission immunity against the evidence provided being used in court against them or their spouse. It does not prevent the evidence being used against a company. Currently, where a person is required to provide evidence or information to the Commerce Commission under the FTA they have the same privileges as witnesses have in any court.

Proposal

MCA considers that there is merit in amending the Fair Trading Act so that a person can be required to appear before the Commerce Commission and give evidence, with appropriate immunity provisions.

Banning Orders

Issue

Under the Fair Trading Act (FTA), an individual can be fined up to \$60,000 for contravening the legislation. Being fined for breaching the FTA, however, does not prevent a person from continuing to supply goods and services. Even when a person has been found to have contravened the FTA on more than one occasion they are still able to trade.

The activities of Michael Knight are a good example of the limitations of the current enforcement provisions and of the potential value of banning orders. In 1994, the Commerce Commission obtained interim injunctions from the High Court relating to alleged breaches of the Fair Trading Act by two companies promoted by Knight. Following that, Knight transferred his business activities to Australia and was there investigated by consumer protection authorities in relation to numerous promotions. Eventually, in New South Wales he was banned for life from trading and in Queensland he was restrained from engaging in trade or commerce relating to the tourism industry.

On Knight's return to New Zealand, he was convicted in April 2002 of a total of thirty three breaches of the Fair Trading Act related to the businesses Budget Imports and Francais Imports Limited. However, in 2001, Knight had been declared bankrupt, thus the court was left with virtually no ability to sentence him. He was fined a total of \$3,000 plus \$130 court costs. The sentencing judge commented, "this is a scam. The result is that a lot of people lost money. Michael Knight displays a total absence of remorse, which is evident here in court today. Under the Fair Trading Act, I have no choice but to fine Knight. You can't expect me to do nothing". The judge also stated, "the reality was Michael Knight's ability to pay was virtually nil and for that reason alone, the fine was a nominal amount".

Knight was also sentenced in July 2004 for 12 further charges of breaching the Fair Trading Act arising from his involvement with another company. On this occasion Knight was fined \$22,000 plus \$6,430 in costs.

The ability of an individual to supply goods and services after breaching the FTA on more than one occasion contrasts with the provisions found in other New Zealand business legislation and in the consumer protection legislation in some of the Australian states.

For example, under the Credit Contracts and Consumer Finance Act 2003 (CCCFA), which like the Fair Trading Act is administered by the Ministry of Consumer Affairs and enforced by the Commerce Commission, persons can be ordered not to act as creditors, lessors, transferees, or buy-back promoters (section 108). The orders are made by the District Court and any person (including the Commerce Commission) can apply to the court for an order. Orders may be made for a specified time or without any time limit and may be made on any other terms or conditions that the District Court thinks fit. Orders can be cancelled or varied at any time by the District Court.

Under the Insolvency Act, without the leave of the court, a bankrupt is prohibited from entering into or carrying on any class of business either alone or in partnership with any person, from acting as a director or taking part directly or indirectly in the management of any company or class of company. The Act also prevents a bankrupt from being engaged in the management or control of any business carried on by or on behalf of, or being in the employ of, persons related to the bankrupt (as identified in section 111(1)(b)). Such a prohibition may be for a specified time period or may be without any time limit. The court may at any time cancel or vary any such order.

Under the Companies Act, the registrar may prohibit persons from being a director or promoter of a company or being concerned (either directly or indirectly) with the management of a company for a period of up to five years. The registrar may exercise this power in relation to persons who have been a director or were involved in the management of two or more companies that have been put into liquidation because of inability to pay debts, ceased to carry on business because of inability to pay debts or has entered into a compromise or arrangement with creditors.

Under the Motor Vehicle Sales Act 2003, the District Court may, on application of any person, make an order that bans any person from motor vehicle trading. An order may be made if a person has been convicted of a specified offence but is not banned

from participating in the business of motor vehicle trading³¹ and the District Court considers that the person is not a fit and proper person to participate in motor vehicle trading. The District Court can also make a banning order if it considers that there is sufficient evidence to indicate that the person is not a fit and proper person to participate in the business of motor vehicle trading.

The inability to ban recidivist offenders has been recognised as a weakness of the Securities Act. The Securities Legislation Bill which is currently before Parliament contains banning provisions.

International Comparisons

Under the fair trading legislation in the Australian states of New South Wales and Victoria individuals can be banned from conducting the business of supplying goods or services.

Under the Fair Trading Act 1987 in New South Wales (NSW), if the Director-General is satisfied that a person has in trade or commerce, engaged in any unlawful conduct³² on more than one occasion (whether in NSW or in any other place), the Director-General may, by notice in writing require an individual to demonstrate why they should not be prevented from carrying on a business of supplying goods or services. The person on whom the notice is served has the right to make a written submission to the Director General within a specified time period. Should a submission be received, the Director-General is required to consider it and conduct any inquiries or investigations to which the notice relates as the Director-General thinks appropriate.

After issuing the notice and considering any submissions that may be received, the Director-General may apply to the Supreme Court for an order. The Supreme Court may prohibit the person who is the subject of the order from carrying on a business of supplying goods or services. The order can be for an indefinite period or for a time specified in the order.

Under the Fair Trading Act 1999 in Victoria, the Director-General may issue a notice in writing that asks a supplier to demonstrate why it should be allowed to continue the business of supplying goods or services. The Director-General is able to issue such a notice if he or she has reasonable grounds to believe that the supplier has engaged in conduct that has contravened the Act or the regulations and if the Director-General believes that the supplier will continue to engage in conduct and that there is a danger that a person may suffer harm, loss or damage as a result of that conduct unless action is taken urgently. If the supplier does not respond to the notice within the time specified, the supplier must cease carrying on the business of supplying the goods or services to which the notice relates or any business of a like kind. The

³¹ Under section 68 of the Motor Vehicle Sales Act 2003.

³² Unlawful Conduct means any conduct that constitutes a contravention of the New South Wales' Fair Trading Act 1987 (or would constitute such a contravention if the conduct occurred in New South Wales), whether or not any proceedings have been brought in respect of the contravention.

supplier to whom the notice applies can appeal the decision to the Victorian Civil and Administrative Tribunal.³³

Discussion

The Commerce Commission has identified a small number of individuals who, even when they have been found by the courts to have contravened the legislation, have continued to supply goods or services in a manner which breaches the legislation. For these recidivist offenders, the available penalties do not appear to act as a deterrent. Having a provision that bans serious offenders from supplying goods or services either for a set period of time or indefinitely would prevent them from being able to continually mislead or deceive consumers. The threat of such a provision should encourage businesses to comply with the legislation, particularly when they have been found by the court to have contravened the legislation. If consumers were aware that recidivist offenders under the FTA could be banned from supplying goods and services this should give them more confidence in the market.

Banning recidivist offenders under the FTA from supplying goods or services would affect the livelihood of these individuals. The impact that these recidivist offenders have on consumers by knowingly contravening the FTA is considered, however, to outweigh this matter.

Proposal

MCA considers that there is merit in amending the Fair Trading Act so that recidivist offenders could be banned from supplying goods or services.

³³ The Victorian Civil and Administrative Tribunal was established by the Victorian Civil and Administrative Tribunal Act 1998.

Part 4 – Legislative Differences That Could Be Considered for Adoption

Key differences between the consumer protection legislation in New Zealand compared with that found in Australia, Canada, the United Kingdom and the United States of America that could be considered for adoption are now discussed. The Ministry of Consumer Affairs considers that these provisions are not a priority at this stage, as there would need to be a regulatory impact analysis, including a cost-benefit analysis, before the proposal could be progressed. The Ministry of Consumer Affairs, however, welcomes your views on these legislative differences and would like to receive any information that you may have on the advantages and disadvantages associated with adopting these provisions into our legislation.

Broadening the Consumer Definition to Include Small Businesses

New Zealand's Consumer Guarantees Act 1993 (CGA) provides for rights and remedies with respect to transactions involving the provision of goods and services to a consumer. A consumer is defined as a person who acquires goods or services of a kind ordinarily acquired for personal, domestic, or household use or consumption and those goods and services are not to be on-sold, used in the course of a process of production or manufacture, or used repairing or treating in trade other goods or fixtures on land.

In the Australian Trade Practices Act 1974 (TPA), a wider definition of consumer is used. The TPA defines a consumer as a person who has acquired particular goods where the price of the goods does not exceed A\$40,000 (regardless of the nature of their use) or, if the price exceeds A\$40,000, the goods were of a kind ordinarily acquired for personal, domestic or household use or consumption. The goods can also be a commercial road vehicle. However, the person must not have acquired the goods, or hold himself or herself out as acquiring the goods, for the purpose of re-supply or for the purpose of using them up or transforming them, in trade or commerce, in the course of a process of production or manufacture or of repairing or treating other goods or fixtures on land.³⁴

The difference between the definitions of consumer in the CGA and TPA is that, under the TPA, businesses, and particularly small businesses, are considered to be consumers for the purposes of that Act. The Australian definition was amended in 1977 to include businesses as a result of the Swanson Committee report. This report concluded that the definition of consumer should be sufficiently broad to provide protection for a range of business transactions, particularly purchases by small businesses. It was felt that the objective of the consumer protection provisions of the TPA was to address inequalities in technical expertise required to negotiate a fair bargain, and that these inequalities are not necessarily limited to "traditional" consumers or transactions involving "consumer" goods. The monetary limit of

³⁴ Similar conditions apply to services.

\$40,000 was suggested as a way of ensuring that most purchases by small businesses are captured under the legislation and those by big business are not.

In 1990, the New Zealand government agreed that transactions involving consumer goods and services should not be identified by way of monetary limits but rather that the test would be whether the goods are of a type ordinarily supplied for private use or consumption, excluding consumers acting in the course of a business or holding themselves out as doing so. The government considered that the ordinary use test more clearly focussed on consumers as opposed to a monetary limit test, and that it was important that the legislation did not cover commercial transactions. Consumer law is based on the need to protect the weaker party, and it was considered that in many commercial transactions there is no weaker party.

Despite the differences in definition, both the Australian and New Zealand courts agree that although most people may use a good for a commercial purpose, if it can be ordinarily used as a domestic product, then the purchaser can be a consumer and the remedies available under the CGA apply. For example, a person who purchases a utility vehicle usually used for farming can be considered a consumer as people now purchase such vehicles for domestic use (*Nesbit v Porter* [2000]).³⁵

In the United Kingdom and Europe, a consumer is defined as “a natural person who is acting for purposes outside his trade, business or profession”. This definition is not considered to be adequate for the CGA provisions as it does not define the type of goods or their use.

A consumer is not defined in the Competition Act in Canada but in provincial consumer protection legislation definitions of a consumer or a buyer are provided. These are not as specific as the definitions in the New Zealand CGA or Australian TPA, and would not adequately meet the purpose of the CGA.

The Ministry of Consumer Affairs is not aware of any information that suggests that New Zealand consumers have been disadvantaged because of the different consumer definition used in the CGA in comparison to the TPA. The main impact would appear to be where businesses are considered consumers and can claim redress as consumers.

Amending the CGA to cover business to business transactions would alter the purpose of the Act, which is to provide protection for consumers and does not cover business-to-business purchases. There is a need to explore the relationship between small and large business transactions but not by broadening the CGA definition of consumer. It is more appropriate that this issue is considered in the review of industry-led regulation presently being progressed by the Ministry of Consumer Affairs³⁶ or possibly in a future review of the Sale of Goods Act 1908.

³⁵ Note that the opposite does not apply. A domestic product used for a commercial use is not covered by the CGA.

³⁶ For further information on the industry-led regulation review (including codes) please refer to the *Review of Industry-Led Regulation* discussion paper [www.consumeraffairs.govt.nz/policyresearch/industry-led-regulation/].

Industry Codes of Conduct

In New Zealand, industry codes of conduct are usually developed by industry associations to regulate the behaviour of their members. They are a form of self-regulation. Typically, standards of conduct identify how a particular industry can comply with the legislation or provide for a level of compliance beyond that required by the legislation. Compliance with a code is usually voluntary.

By joining an industry association which uses a code, a trader agrees to conduct their business according to that code. The code is created by the association in consultation with its membership and other organisations, as necessary. Breaching a code can result in sanctions and penalties, which may include revocation of membership. As membership usually confers some form of benefit to the trader, (for example, prestige) the threat of membership revocation may deter a trader from operating outside the code.

In Australia and in the United Kingdom, codes are specifically provided for in the consumer protection legislation. The process that is used is different, however, and while in Australia the code provisions can cover competition or consumer issues, the consumer codes approval scheme provided for by the Enterprise Act 2002 in the United Kingdom is specifically designed for the benefit of consumers.

The Australian Trade Practices Act (TPA) provides for industry codes to be prescribed in regulation. Codes must be declared to be either mandatory or voluntary. Compliance with a prescribed voluntary code applies only to those businesses that subscribe to the code. Prescribed mandatory codes are mandatory on all businesses covered by the code.

In the TPA, there are specified remedies and penalties if an industry code is contravened. The Australian Competition and Consumer Commission can enforce mandatory codes by administrative methods, such as undertakings or through the courts. The courts can grant injunctions, award damages and make various orders (including non-punitive). Currently, the franchising code is the only mandatory code that is prescribed under the TPA. There are no prescribed voluntary codes.

In the United Kingdom, the Enterprise Act provides the Office of Fair Trading (OFT) with increased powers to assist in the development of effective self-regulation by the approval and promotion of consumer codes of practice that meet the OFT's core criteria. The Consumer Codes Approval Scheme (CCAS) consists of two stages. Stage 1 requires the code sponsor to make a promise that their code meets OFT's published criteria for codes. At stage two, the code sponsor has to demonstrate, with evidence, that their code is working in practice and that it delivers on that initial promise. OFT endorsement and promotion of the code begins once the burden of proof has been met by the code sponsor.

The OFT publicises the fact that a code has completed stage one and following the completion of stage two and the granting of an approval, the code is promoted³⁷ by

³⁷ Being a member of an approved code does not make a business immune to enforcement action should evidence suggest that it has breached the law.

the OFT as part of the CCAS. Monitoring of the effectiveness of the code continues post approval and is conducted by both the code sponsor and the OFT.

The main aim of the CCAS is to safeguard consumer interests and to provide benefits to consumers through OFT approved codes that go beyond the requirements in the law. The OFT admits that the criteria are challenging and that meeting them requires considerable commitment from the code sponsors and their members in order to successfully complete the process and obtain approval. The OFT also acknowledges that not all code sponsors who apply will be able to achieve approval for their codes.

In New Zealand, neither the Commerce Commission nor the Ministry of Consumer Affairs have any formal role in endorsing industry codes.³⁸ The Ministry of Consumer Affairs, however, has guidelines for industry on self-regulation and has been involved in advising different organisations on self-regulation schemes related to consumer complaints and redress.

The Ministry of Consumer Affairs is currently conducting a review on industry-led regulation. It is appropriate that any proposals relating to codes of conduct be made as part of this review. For further information on the industry-led regulation review (including codes) please refer to the *Review of Industry-Led Regulation* discussion paper [www.consumeraffairs.govt.nz/policylawresearch/industry-led-regulation/].

Super-Complaints

The Enterprise Act 2002 in the United Kingdom allows designated³⁹ consumer groups to submit super-complaints to the Office of Fair Trading (OFT) on issues that affect many consumers. To ensure that these super-complaints contain the required information, the process that must be followed by the designated agencies before a complaint can be made is demanding.

When the OFT receives a super-complaint, it has a duty to investigate the complaint within 90 days and must publish a response stating what action, if any, it intends to

³⁸ The *Government Policy Statement on Electricity Governance* 2004 requires that the Electricity Commission in consultation with the Ministry of Consumer Affairs develop certain electricity industry codes. Compliance with the *Government Policy Statement* is a requirement under the Electricity Act 1992.

³⁹ To become a designated super-complaints body, a consumer group must meet certain criteria, such as:

- is known to represent the interests of consumers and is suitably independent, impartial and has integrity. evidence of this includes CVs of the directors, financial accounts, etc;
- demonstration of considerable experience and competence in representing the interests of consumers;
- the ability to put together reasoned super-complaints;
- willingness to co-operate with the OFT and other agencies; and
- procedures are in place to ensure there is no conflict of interest if the body has commercial interests.

take. Such action can include no further action, a finding that the complaint was unfounded, dismissal of the complaint as frivolous or vexatious, a referral of the complaint to a more relevant regulator or enforcement action by OFT's consumer regulation division.

The super-complaints provision is a fast-track system designed to ensure that complaints about market failure are considered within a specified period of time.

Although the super-complaints system is regarded as a success in the United Kingdom, it is not proposed that the Fair Trading Act (FTA) be amended to provide for such a system in this country. This is because the benefits that have accrued in the United Kingdom since the introduction of the super-complaints system would be unlikely to occur in New Zealand. In the United Kingdom complaints received about consumer protection issues are directed to Trading Standards Authorities (TSA). There are 202 of these. It can, therefore, be difficult for the TSAs to recognise when a number of consumers throughout the country have been affected by a particular trader or where a market failure may be occurring. In New Zealand, in contrast, the Commerce Commission has a centralised complaints processing system which handles all the complaints received by the Commission.

In addition, implementation of a provision similar to the super-complaints system in New Zealand would require significant adaptation to the New Zealand situation. Many of the designated consumer groups in the United Kingdom have government funding or are funded by levies, thereby providing them with the resources to undertake research and policy development. No consumer group in New Zealand is funded in such a way. This is likely to impair their ability to be make super-complaints

Adopting a super-complaint system would also have implications for the Commerce Commission. The Commerce Commission is an independent Crown entity. It is funded by the government but the government cannot direct the Commerce Commission to investigate particular complaints. Instead the Commerce Commission identifies the market areas that it will investigate as a matter of a priority. Requiring the Commerce Commission to investigate particular complaints brought to its attention by consumer groups within a specified timeframe may affect the Commission's ability to focus on the areas that it has identified as priorities based on its own monitoring of the market and the complaints that it receives.

Before a super-complaint system could be proposed, there would need to be significant information that indicates that the current system would be greatly improved by the introduction of such a provision in the FTA. Currently, there are informal arrangements between consumer groups and the Commission to discuss where consumer groups see priorities and how the Commission's priorities compare. Some of the recent Fair Trading Act court cases taken by the Commerce Commission have originated from information supplied to the Commerce Commission by consumer organisations.

Formal Cautions

The Office of Fair Trading and the Trading Standards Authorities in the United Kingdom can, in accordance with the Enforcement Concordat⁴⁰ issue formal cautions. Formal cautions are used as an alternative to prosecution and are the same as police formal cautions. Cautions are recorded on the Central Register of Convictions and are used to deal with less serious offenders in an attempt to reduce re-offending. If an individual re-offends within three years of receiving a caution, this can be taken into account if he or she is prosecuted.

Before a caution can be given, there must be sufficient evidence to suggest that a conviction is a realistic prospect. The suspected offender must admit to the offence (in writing) and give informed consent to the caution.

Formal cautions are not used in New Zealand although the police do have the power to use diversion. Under the diversion power, offenders are charged (that is, police lay an information), but then are diverted from the court processes by agreeing to conditions (a form of undertaking).

As the New Zealand Police do not have the power to issue formal cautions and the New Zealand penalty system differs from the United Kingdom, this matter will not be investigated further and it is proposed that formal cautions not be provided for under the Fair Trading Act.

Unconscionable Conduct Prohibition

Unconscionable conduct is generally defined to be when one party subjects another party to undue pressure to enter into a transaction, i.e. if a business takes advantage of a consumer's physical or mental infirmity, ignorance, illiteracy, age or inability to understand the nature or language of the transaction. It can also apply to the business's knowledge about the consumer's ability to pay for the product or service.

Unconscionable conduct is not specifically provided for under the Fair Trading Act (FTA).⁴¹ Unconscionable conduct is, however, covered by the Disputes Tribunals Act 1988⁴² and common law. Consumers currently have to take court action for themselves if affected by unconscionable conduct. Under the Disputes Tribunals Act section 19 (1) (e) and (f), Disputes Tribunals referees have a wide jurisdiction to deal with unconscionable contracts:

(e) Where it appears to the Tribunal that an agreement between the parties, or any term of any such agreement, is harsh or unconscionable, or that any power conferred

⁴⁰ The Enforcement Concordat [www.cabinetoffice.gov.uk/regulation/enforcement_concordat/] is a document produced by the United Kingdom Cabinet Office that outlines rules of enforcement.

⁴¹ The Credit Contracts and Consumer Finance Act 2003 (CCCFA), which is also enforced by the Commerce Commission, has a part that focuses on the reopening of oppressive credit contracts, consumer leases and buy-back transactions. Under the CCCFA, oppressive is defined as "harsh, unjustly burdensome, unconscionable, or in breach of reasonable standards of commercial practice".

⁴² The Disputes Tribunal can hear claims up to \$7,500 (or \$12,000, if both parties agree).

by an agreement between them has been exercised in a harsh or unconscionable manner, the Tribunal may make an order varying the agreement, or setting it aside (either wholly or in part);

(f) Where it appears to the Tribunal that an agreement between the parties has been induced by fraud, misrepresentation, or mistake, or any writing purporting to express the agreement between the parties does not accord with their true agreement, the Tribunal may make an order varying, or setting aside, the agreement or the writing (either wholly or in part).

In Australia, unconscionable conduct is covered by both common law and statutory unconscionable conduct provisions in the Trade Practices Act 1974 (TPA) and in some state legislation. The unconscionable conduct provision was introduced into the TPA in 1979 because it was considered that while some conduct may not be misleading or deceptive, it could be unfair or unreasonable. There are two statutory prohibitions against unconscionable conduct at the federal level: one for consumer transactions (relating to goods and services that are ordinarily used for domestic or household use), and one for business transactions to protect small businesses. Only civil remedies are available for breaches of these provisions. Penalties include injunctions, damages and compensatory orders, and the contract or part of the contract can be made void.

Unconscionable conduct is also written into some provincial Canadian legislation and can include terms or conditions which are so harsh or adverse to the consumer as to be inequitable. Remedies include making the transaction non-binding on the consumer.

Whether action is taken by an individual or an enforcement agency under either common or statutory law, the decision as to whether unconscionable conduct has occurred is made by the court.⁴³ Therefore, seeking redress and enforcement against unconscionable conduct is often expensive. Penalties are usually the same as those that apply when a business breaches any of the unfair practices' provisions.

In the 20 years since the passing of the FTA, the addition of unconscionable conduct provisions has been raised several times. While there are obvious advantages to consumers associated with the addition of specific unconscionable conduct provisions, further work has never progressed. This appears to be because unconscionable conduct can be difficult to prove and also because such amendments to the FTA would have implications beyond that legislation.

Amending the FTA so that unfair terms in consumer contracts were specifically prohibited (as discussed earlier in this paper) should benefit consumers in a timely manner while reducing the number of potential unconscionable cases. Therefore amending the FTA to specifically provide for unconscionable conduct provisions is not being proposed.

⁴³ The Ministry of Consumer Affairs understands that the Australian Competition and Consumer Commission has recently settled with several parties who have admitted that their behaviour was unconscionable.

Part 5 - Submissions

MCA welcomes submissions on the proposed amendments to the Fair Trading Act 1986 as outlined in part three of this discussion paper. Please clearly identify which proposal(s) you are commenting on in your submission.

MCA also welcomes any comments that you may have on the legislative differences that could be considered as discussed in Part 4 of this paper.

Please forward submissions to:

Enforcement Review
Policy Unit
Ministry of Consumer Affairs
PO Box 1473
Wellington
Email: enforcement-review@mca.govt.nz
Telephone 04-474 2944 or 04-462 4273
Fax 04-473 9400

The closing date for submissions is **29 June 2006**.

Official Information Act 1982

Please note that any submission that you make may become publicly available under the Official Information Act 1982. If you feel there is any part of the submission that should not be publicly available, please indicate this clearly in your submission.

References

Ayres, I. and Braithwaite, J. 1992, *Responsive Regulation: Transcending the Deregulation Debate*, Oxford University Press, Oxford.

Gilligan, G., Bird, H. and Ramsay, I. 1999, *The Efficacy of Civil Penalty Sanctions Under the Australian Corporations Law, Trends and Issues*, Australian Institute of Criminology, Canberra.

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