Consumers benefit from transparency

Proposed changes to the *Fair Trading Act* strengthen the position of consumers when it comes to dealing with "unfair" contracts. By James Catlin

Unfair contracts amendments to the *Fair Trading Act* 1999 (*FTA*) proclaimed on 9 October 2003 are a revolutionary advance on consumer protection provisions currently available under the *FTA*, the *Trade Practices Act* (*TPA*) and common law.

Australia's legal framework deals with unfairness almost exclusively in a procedural sense in the creation of a contract rather than the unfairness of a contract *per se*. The *Fair Trading Act (Amendment) Bill* 2003 changes this scenario dramatically by striking at terms that cause "a significant imbalance in the rights and obligations under a contract to the detriment of the consumer".

The amendments are closely modelled on UK legislation which has had a significant impact there. The *FTA* is also significant in leaping ahead of developments in the law of unconscionability and tentative attempts by the common law to define and imply terms of good faith. The new rights do not require special disadvantage or wrongful conduct in a contract's formation as such but rather impose positive obligations on suppliers to make contracts fair. The significant provisions of the new Part 2B of the *FTA* are discussed in this article.

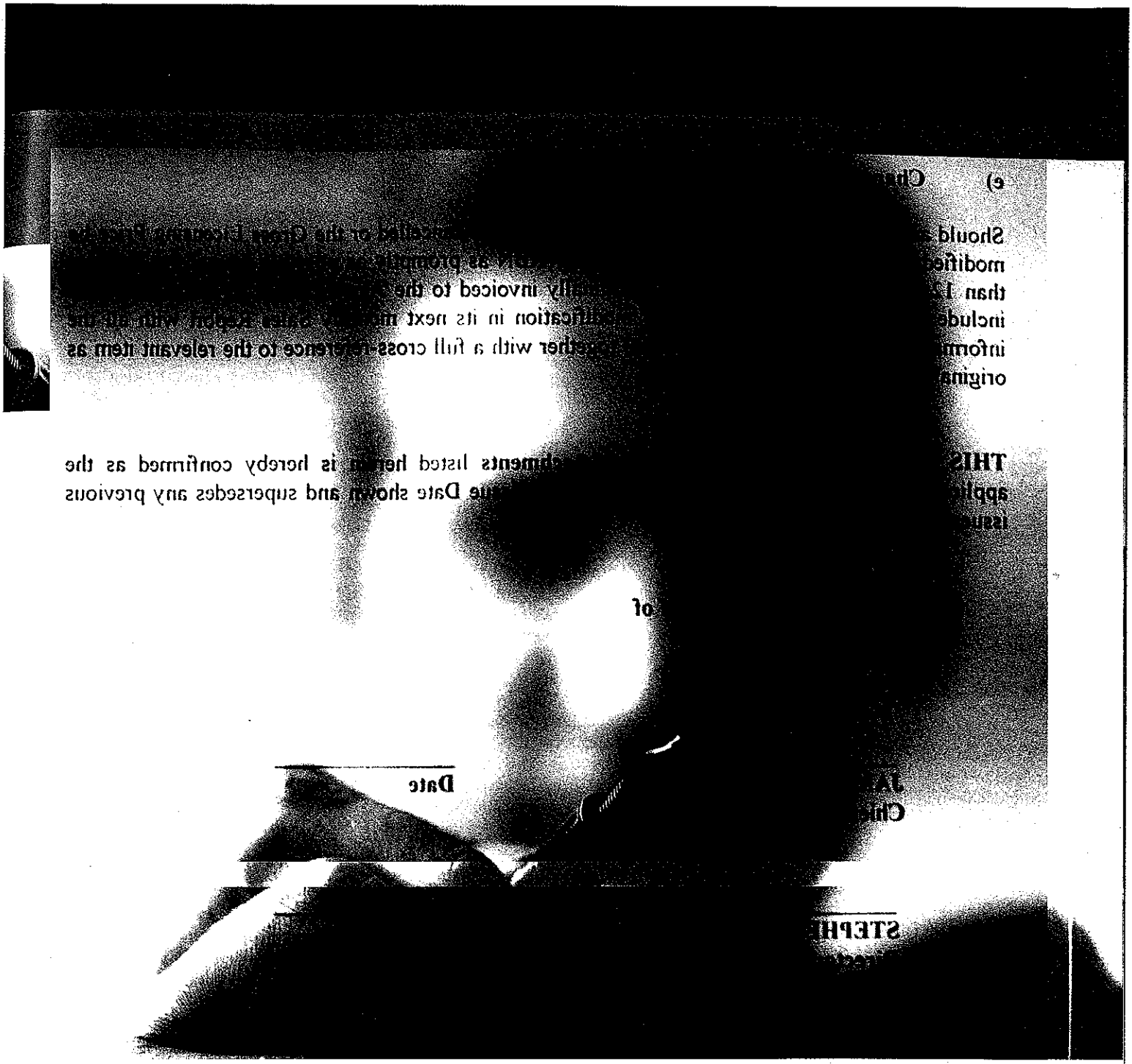
Section 32W defines a contractual term as being unfair if:

"Contrary to the requirements of good faith and in all the circumstances, it causes a significant imbalance in the parties' rights and obligations arising under the contract to the detriment of the consumer".

The contracts affected remain those generally governed by the *FTA*, goods and services of a kind ordinarily acquired for personal or domestic use.

What is unfair ?

The *FTA* provides helpful guidance on the slippery concept of "fairness" in s32X which provides that:



"A court or tribunal may take into account, among other matters, whether the term was individually negotiated, whether the term is a prescribed unfair term and whether the term has the object or effect of:

(a) permitting the supplier but not the consumer to avoid or limit performance of the contract;
(b) permitting the supplier but not the consumer to terminate the contract;
(c) penalising the consumer but not the supplier for a breach or termination of the contract;
(d) permitting the supplier but not the consumer to vary the terms of the contract;
(e) permitting the supplier but not the consumer to renew or not renew the contract;
(f) permitting the supplier to determine the price without the right of the consumer to terminate the contract;
(g) permitting the supplier unilaterally to vary the characteristics of the goods or services to be supplied under the contract;
(h) permitting the supplier unilaterally to determine whether the contract had been breached or to interpret its meaning;
(i) limiting the supplier's vicarious liability for its agents;
(j) permitting the supplier to assign the contract to the consumer's detriment without the consumer's consent;
(k) limiting the consumer's right to sue the supplier;
(l) limiting the evidence the consumer can lead in proceedings on the contract; and
(m) imposing the evidential burden on the consumer in proceedings on the contract".

While this section looks comprehensive, it is easy to see how there is considerable room for interpretation within each subsection as the overriding test governing each of the objects or effects set out in s32X(a)-(m) is whether a significant imbalance in the parties' rights has arisen contrary to the requirement of good faith. For example, every contractual term allowing a supplier to "vary characteristics or price of a good or service supplied" (s32X(g)) does not necessarily cause a significant imbalance in the rights of the consumer if it is in good faith.

Despite the generic use of the term "unfair", the test remains twofold – a term must be:

- contrary to the requirements of good faith; and
- result in a significant imbalance in the parties' rights and obligations.

Whether a term is essential or fundamental is subsumed in the question of significant imbalance as a non-core term may not affect relative rights significantly.

Good faith

The equal use of both criteria of contrary to good faith and significant imbalance in rights is not without controversy despite that being the statutory approach taken in the UK.[1] The law of good faith itself has been described as being in a state of utter confusion.[2]

The UK Law Commission has identified different interpretations as to how the two criteria interrelate.[3]

One interpretation characterises good faith as a matter of procedural fairness and significant imbalance as a matter of substantive fairness but gives both tests equal weight. Another characterises good faith as the substantive test. Australian common law has been moving toward implication of a term of good faith in contracts but what that term means is still unclear. Recital 16 of the EU Directive, which was the basis of the UK regulation, provides that the following are considerations in deciding on the existence of good faith:

- strength of bargaining position;
- whether the consumer had an inducement to agree to the term;
- whether the product was sold to the special order of the consumer; and
- whether the supplier dealt fairly and equitably with the consumer.

Without codification good faith is a philosophical quagmire.[4]

Imbalance in rights and obligations

The expression "significant imbalance in the parties' rights and obligations" has not been defined. The issues a court might consider if it was required to assess significant imbalance as a separate issue (i.e. a defence that there was no significant imbalance) might include:

(a) what a consumer would normally expect from a contract of the type in question;
(b) previous dealings by the consumer;
(c) whether the consumer knew of the term; and
(d) opportunity to read and comprehend the term.

Guidance by Consumer Affairs Victoria is unlikely to prevent a considerable body of case law developing on the interpretation of the imbalance and good faith tests, individually and in combination.

Effect of unfairness

Unfair terms in contracts with these characteristics are void although the contract remains on foot "if it is capable of existing without the unfair term" (s32Y).

Section 32X makes some distinction between contracts negotiated individually and standard form contracts but the weight to be put on this distinction is unclear. Section 32 says only that the court may take individual negotiation "into account".

Implicit in these reforms is the premise that consumers have no say in a standard form contract and in reality have no discretion to amend it due to a relative imbalance in the power of the consumer. Individually negotiated contracts are a different matter which would presumably remain subject to common law conceptions of freedom of contract, economic freedom and *caveat emptor*.

The UK Act[5] from which the Victorian reforms are derived clearly excises negotiated terms from the statutory regime. It is open for Victorian courts to fill the gap in statutory language. The *FTA* could have simply stated that individual negotiated terms are outside the regime and has not done so.

Standard form contracts will also be retrospectively affected if the Governor-in-Council prescribes them to be unfair by regulation. The Director of Consumer Affairs Victoria may apply to the Victorian Civil and Administrative Tribunal (VCAT) for a declaration that a term of a standard form contract is a prescribed unfair term. As with the rest of the *FTA*, VCAT shares jurisdiction with other courts in the application of s32Y rendering unfair terms void. VCAT, however, has exclusive jurisdiction on the declaratory and injunctive aspects of Part 2B of the *FTA*.

The penalties for breach at this stage are relatively light – $1000 for a person and $2000 for a company, and these only apply to prescribed unfair terms. However, as the penalties apply per contract involved, and given the volume of standard form contract use, breaches of the *FTA* would tend to attract multiple fines.

My reading of the amendments indicates the following clauses will be at least suspect under the changes:

- formality requirements: compliance by the consumer with some unimportant or obscure formality as a precondition to meeting a supplier's commitments;
- exclusion of liability clauses: these are currently void per s97 of the *Goods Act* 1958 and s68 of the *TPA*, although s68A allows such terms if they are "fair and reasonable";
- terms that allow the supplier to retain prepayments on the consumer's cancellation of the contract;
- terms that have the effect of automatically extending a contract of fixed duration;
- entire agreement clauses – i.e. clauses that exclude liability for words spoken that do not appear in the contract;
- exclusion of consumers' right to assign what they purchase;
- terms which say the supplier is liable only to the extent that he can claim against the manufacturer;
- terms which exclude liability for delay or allow unduly long periods for delivery or completion of work;
- a requirement to pay more in compensation for a breach than is reasonable – pre-estimate of loss caused by a supplier; and
- entire agreement clauses, i.e. that no pre-contractual representations have been relied on.

Entire agreement clauses already have questionable effectiveness under the *TPA* and arguably the *FTA* depending on whether they are exclusion clauses.[6]

The impact of these amendments will depend in part on how proactive the Director of Consumer Affairs Victoria chooses to be. He has the power to institute proceedings on behalf of a consumer against a trader (s105). Consumer Affairs Victoria can be expected to already have a number of significant standard form contracts in its sights.

At a conference to introduce the legislation held on 7 November, the Director indicated that Consumer Affairs Victoria had particular interest in the following industry sector contracts: utilities, telecommunications (particularly mobile telephony in relation to youth contracts) home removalists the building industry, the fitness industry retirement homes, Internet providers and car hirers.

The Director also has the power to seek "advisory opinions" from VCAT under s32ZD "on any matter, including but not limited to:

(a) whether a contract is a consumer contract or standard form contract;

(b) whether a term of a consumer contract is an unfair term; or
(c) whether a term of a standard form contract is a prescribed unfair term".

The Director has the power to prompt self-reform by seeking information from a company or person about its contracts. Under s32ZB, the Director may "require any person to supply . . . a copy of a document (a) or information about the use or recommendation for use by that person of that document in dealings with consumers". Compliance with this section is bolstered by a maximum fine of $6000 for failure to comply. The UK Office of Fair Trading has negotiated changes in more than 5000 contractual terms.

Economic fairness

What if unfairness in the sense of the s32X categories is argued to be offset by a relatively low price or good economic value? The UK regulations specifically remove price as a consideration in unfairness (s6). The *FTA* does not.

The *FTA* places the concept of significant imbalance in the parties' rights in the context of "all the circumstances" and as a matter of statutory interpretation provides for economic considerations.

How economic arguments will be treated by the courts and Consumer Affairs Victoria is unclear. Take, for example, standard term exclusion clauses in transport and courier contracts that essentially enable a company transporting goods to destroy them by accident or lose them and be protected from any legal proceeding.[7] A clear body of case law has deemed these clauses to be binding. An economic logic and insurance practice has built up around them. Insurance for goods is generally paid for separately as a transparent extra charge. Will these exclusion clauses be saved by an economic component to fairness? Similarly, "Himalaya" clauses protecting a sub-contractor have been upheld by the courts[8] but would appear to be *prima facie* void under s32X(i) "limiting the supplier's vicarious liability for its agents".

Goodbye fine print

A considerable body of law governing whether a consumer has notice of a term in a contract has developed partly in response to the phenomena of "the fine print" or potent terms in text that is commonly unreadable without a magnifying glass. Section 163(3) mandates that a consumer document must be:

- easily legible;
- to the extent that it is printed or typed uses a minimum of 10-point font; and
- clearly expressed.

Fines are $12,000 for a company and $6000 for individuals for a breach of this term.

The meaning of clear need not be limited to size and shape of words but includes whether jargon or terminology with which the average consumer is unfamiliar has been used.

This provision is unlikely to make case law on adequate notice of contractual terms obsolete. The "ticket cases" where Australian courts gave consideration to whether a customer has reasonable notice of a clause have involved considerations such as:

- whether the consumer has been part of the transaction and associated contract before;
- whether notice boards alerted the consumer to an important term; and
- whether the supplier or service provider has otherwise alerted the consumer to the term.[9]

These considerations will still apply.

These reforms easily overtake unconscionability as a legal principle protecting consumers in commercial transactions on the basis of disadvantage whether arising out of statute or common law. While unconscionability principles have been expanding[10] to cover more transactions they have remained narrowly based on wrongful conduct or special disadvantage during negotiation such as age, language difficulties, and reliance arising out a relationship. These unconscionability principles include notions of good faith and have some statutory overlap with unfairness under the *FTA*:

(a) relative strengths in bargaining position of corporation and consumer: *TPA* s51AB(2)(a); *FTA* s8A(3)(a); and *Contract Review Act* 1980 (NSW) (*CRA*) s9(2)(a); and
(b) whether a term is reasonably necessary for the protection of the legitimate interests of the supplier: *TPA* s51AB(2)(b); *FTA* s8A(3)(b); and *CRA* s9(2)(d).

The *CRA*'s unjust contract provisions have been interpreted, however, as relating to procedural unfairness. The explanatory memorandum accompanying s51AA's introduction as law stated that "the equitable principles of unconscionable conduct do not embrace conduct which, with nothing more is merely unfair or unreasonable, or which merely amounts to a hard bargain".

These new provisions do and have a lower threshold of unfairness to satisfy in order to obtain relief. The new unfairness provisions also bypass the question of bargaining strengths by virtually deeming the consumer's weak bargaining position to be a basis for relief whenever contractual terms coming within the s32X categories arise in a contract. Looking at *TPA* s51AC which is much more expansive, it is easy to see how the *FTA* takes a clear new direction in legislative approach. While there has for some time been a recognised implied duty in contracts on parties of good faith and fair dealing,[11] the boundaries of that duty are vague and controversial and the High Court is waiting to rule definitively on them.[12]

Soon to be national

Other states are likely to follow these reforms given positive indications at meetings of the Ministerial Council on Consumer Affairs and the Standing Committee of Officials of Consumer Affairs. The UK regulations themselves were promulgated to give effect to a Directive on Unfair Terms in Consumer Contracts issued in 1993 by the European Council of Ministers. These reforms therefore are part of a clear international trend. ●

JAMES CATLIN is a member of the Victorian Bar, practising in commercial law, criminal law, defamation, media and entertainment law. This article is extracted from a paper presented at Wisewoulds, Russell Kennedy and Tress Cocks and Maddox.
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1. Section 5, *Unfair Terms in Consumer Contracts Regulations* 1999.
2. Carter, JW and Peden, E, "Good faith in Australian contract law" (2003) 19 *Journal of Contract Law* 155.
3. "Unfair terms in contracts: a joint consultation paper", The Law Commission (CP no 166), paras 3.57–3.62.
4. But see also Ian Stewart, "Good faith in contractual performance and in negotiation" (1998) 72 *ALJR* 370 for matters such as: refusing to disclose relevant information, rejecting routine terms, shifting bargaining position when agreement is near, engaging in dilatory tactics, withholding agreement on trivial matters, requiring unreasonable or unattainable conditions.
5. Note 1 above.
6. *Clark Equipment Aust Ltd v Covcat Pty Ltd* (1987) 71 ALR 367, Sheppard J at 371.
7. *Thomas National Transport (Melb) Pty Ltd v May & Baker (Aus) Pty Ltd* (1966) 115 CLR 353.
8. *Port Jackson Stevedoring Pty Ltd v Salmond and Spraggon Pty Ltd* (1978) 139 CLR 231.
9. *Sydney City Council v West* (1965) 114 CLR 481.
10. Bryan Horrigan, "Unconscionability breaks new ground" [2002] *Deakin Law Review* 4.
11. *Renard Constructions (ME) Pty Ltd v Minister for Public Works* (1992) 26 NSWLR 234.
12. *Royal Botanical Gardens and Domain Trust v South Sydney City Council* [2002] HCA 5.