Chapter 4

Defining 'unfair' contract terms

4.1 What is an 'unfair' consumer contract term and how do the bill's provisions differ from the 'unconscionable conduct' provisions in section 51AB of the Trade Practices Act? This chapter explores both these issues.

Void and unfair terms

4.2 Subsection 2(1) of the bill states that a term of a consumer contract is void if:

- the term is unfair; and
- the contract is in a standard form contract.

4.3 In the context of the ASIC Act, a term of a consumer contract is void if:

- the term is unfair; and
- the contract is in a standard form contract; and
- the contract is a financial product or a contract for the supply, or possible supply, of services that are financial services.[1]

4.4 Subsection 3(1) of the bill provides that a term in a consumer contract is unfair if the term:

(a) would cause a significant imbalance in the parties' rights and obligations under the standard form contract; and

(b) is not reasonably necessary to protect the legitimate interests of the party who would be advantaged by the term.[2]

4.5 If the court finds that a term is unfair, and therefore void, it is treated as if it never existed.[3] Subsection 2(2) of the bill states that the contract continues to bind the parties if it is capable of operating without the unfair term.

The bill's presumptions

4.6 These sections defining 'unfair' and 'void' contract terms carry two important presumptions. The first is that a contract term is not reasonably necessary to protect the legitimate interests of the party advantaged by the term (subsection 3(4)). The second is that the contract is in a standard form (subsection 7(1)).

---

1 *Explanatory Memorandum*, p. 13 and p. 28.

2 Subsection 3(1)

3 *Explanatory Memorandum*, p. 21.

4.7 Subsection 3(4) of the bill states that:

> …a term of a consumer contract is presumed not to be reasonably necessary in order to protect the legitimate interests of the party who would be advantaged by the term, unless that party proves otherwise.

4.8 The Minister has explained this onus of proof in the following way:

> First, it will be for the party advantaged by a term—usually a business—to rebut the presumption that the term is not reasonably necessary in order to protect its legitimate interests. Second, it will be for a party that asserts that a contract which is the subject of a challenge is not in a standard form—again, usually a business—to rebut the presumption that the contract is in standard form. In both cases, there are issues that the business will know and it will be able to introduce the evidence it considers most appropriate to the question. It would be a huge impediment for an individual claimant to prove either of these matters, as they are unlikely to be able to bring evidence before a court without disproportionate effort and expense. A regulator would need to use intrusive and expensive coercive information-gathering powers to obtain the required information to bring a case.[4]

4.9 Subsection 7(1) of the bill states:

> If a party to a proceeding alleges that a contract is a standard form contract, it is presumed to be a standard form contract unless another party to the proceeding proves otherwise.

Views

4.10 Several submitters expressed concern at these two presumptions. For example, Colonial First State Property Management (CFSPM), a member of the Shopping Centre Council of Australia, criticised the draft bill for allowing:

> …parties to challenge 'standard form contracts' that they once had formally agreed to, on the basis that the terms are unfair, simply because they later don't like the terms and no longer wish to be bound by them. Consequently, the whole notion of businesses being able to rely on their contractual terms with certainty is eroded and exposes them to the very significant risk of vexatious litigants and costly litigation. Such costs will inevitably flow through to the costs of goods and services and in tough economic times, this is the last thing that businesses and consumers need.[5]

4.11 The Australian Bankers' Association commented in its submission to the draft legislation in May that the bill wrongly places the onus of proof with the respondent.

4.12 The National Australia Bank (NAB) argued that the bill's automatic presumption of unfairness is not present in existing unfair contracts legislation

---

4 The Hon. Dr Craig Emerson, Second Reading Speech, *House of Representatives Hansard*, 24 June 2009, p. 6984.

5 *Submission 11*, p. 3,

overseas. It thereby claimed that the provision is 'untested and undermines fundamental principles of contract law'. Instead, the NAB recommended that the bill should have a 'positive test of unfairness' which specifies a 'materiality threshold'.[6]

4.13 The NAB also criticised the bill's reference to 'legitimate interests' for its lack of clarity. It argued that without clarification of these words:

> …the application of the presumption that a term is not reasonably necessary to protect legitimate interests unless proved otherwise destabilises the freedom of commerce and certainty of contract required for efficient commerce.[7]

4.14 The NAB recommended that the bill specify those considerations which can determine a party's legitimate interests, such as 'accommodating technological change'.[8] The ABA also recommended that the bill should provide guidance on the meaning of 'legitimate interests'.[9]

4.15 In its submission to this inquiry, the BCA reiterated the concerns it expressed in its submission in May on the draft provisions:

> The draft proposals reverse the onus of proof. This represents a significant departure from traditional standards of proof in contractual proceedings and therefore requires further consideration, including cost-benefit analysis. A cost benefit analysis should take into account experiences with the operation of a reverse onus of proof such as that in the UK. One commentator has suggested it "has been an area that has created uncertainty in the UK and will be repeated in Australia".[10]

4.16 Mr Ian Tonking SC argued that the bill's approach is flawed. He wrote in his submission that the bill 'appears to be based on the premise that freedom of contract ought to be retained and protected except to the extent that such freedom, because of inequality of bargaining power or other reasons, leads to unfairness in particular cases'. But in practice, the average consumer may either accept the terms of the contract or decline the opportunity; 'the notion that freedom of contract has any scope in this context is fanciful'.[11] Further, he argued, the bill adopts a case by case basis to determine what is unfair.

4.17 Not all the committee's evidence was critical of the presumptions, however. The Consumer Action Law Centre argued that subsection 3(4) is 'sensible and

---

6 National Australia Bank, *Submission 30*, p. 4.

7 National Australia Bank, *Submission 30*, p. 3.

8 National Australia Bank, *Submission 30*, p. 3.

9 Australian Bankers' Association, *Submission 32*, p. 6.

10 Business Council of Australia, *Submission 20*, p. 4. The BCA was citing George Raitt, 'Unfair contracts bill repeats UK problems', *Australian Financial Review*, 23 July 2009, p. 63.

11 *Submission 4*, p. 4.

practical' given it is the party seeking to rely on the term that is in the best position to produce evidence about the term's nature.[12] Similarly, it argued that subsection 7(1) 'is appropriate as it is that party which is in the best position to produce evidence about the way in which it contracts with other consumers'.[13]

Standard form contracts

4.18 As noted, for a contract term to be considered void, the contract must be a standard form (or non-negotiated) contract. Subsection 7(1) of the bill states that if a party to a proceeding alleges that a contract is a standard form contract, it is presumed to be a standard form contract unless another party (typically the respondent) to the proceeding proves otherwise.[14]

4.19 The EM states that if a party wishes to argue that a contract has been negotiated and is not in a standard form (and is therefore not subject to the unfair contract term provisions), then the rebuttable presumption requires the party that presents the contract to show that the contract is not a standard form contract. This reflects the fact that the claimant will usually only have evidence of their own contract, and that the respondent is best placed to bring evidence regarding the nature of the contracts it uses.[15]

4.20 Subsection 7(2) of the bill states that in determining whether a contract is a standard form contract, the court may take into account such matters as it thinks relevant but must take into account:

- whether one of the parties has all or most of the bargaining power relating to the transaction;
- whether the contract was prepared by one party before any discussion relating to the transaction occurred between the parties;
- whether another party was, in effect, required either to accept or reject the terms of the contract (other than the terms referred to in section 5(1)) in the form in which they were presented;
- whether another party was given an effective opportunity to negotiate the terms of the contract that were not the terms referred to in section 5(1);
- whether the terms of the contract (other than the terms referred to in section 5(1)) take into account the specific characteristics of another party or the particular transaction; and
- any other matter prescribed by the regulations.

---

12 Consumer Action Law Centre, *Submission 19*, p. 5.

13 Consumer Action Law Centre, *Submission 19*, p. 9.

14 Subsection 7(1)

15 *Explanatory Memorandum*, p. 29.

4.21 The relevant Minister may add to this list through regulations.[16]

Views

4.22 The Consumer Action Law Centre supports the bill's non-prescriptive definition of a standard form contract. It argued that a more prescriptive definition would 'simply provide opportunities for avoidance'.[17]

4.23 Others saw this lack of definition as problematic. Mr Tonking SC argued in his submission that:

> …s.7 includes a rebuttable presumption that any contract asserted by a party to be a standard form contract is a standard form contract unless another party proves otherwise. While the question whether a particular term is a prohibited term may in many instances be beyond dispute, the question whether a particular contract is a standard form contract may well be a matter of dispute.[18]

4.24 In similar vein, the property manager CFSPM has noted that the bill fails to define a standard form contract 'and gives no guidance on how much negotiation over terms must occur before a contract is not considered 'standard'. It explained that retail leases are not 'standard form contracts' and to suggest that they are is 'patently wrong'. Nonetheless, under the provisions of the bill, property managers like CFSPM would face the additional expense of proving that a contract is not 'standard' 'at the whim of a judge'.[19]

4.25 The NAB suggested that the government should delete subsection 7(1) of the bill, and should define a standard form contract in the following terms:

> …contracts that substantially comprise terms and conditions similar to contracts entered into by the supplier for similar goods and services and which meet the elements of a standard form contract set out in section 7(2).[20]

4.26 ABACUS has argued that the bill should not only exclude terms that are part of non-standard form contracts, but also to exclude negotiated contract terms. As it wrote in its submission:

> …if there has been a genuine negotiation of a particular term, a party to that negotiation should not be able to avoid that term just because, taken

16 *Explanatory Memorandum*, p. 30.

17 Consumer Action Law Centre, *Submission 19*, p. 9. The Centre also argued that there is 'little reason' why the bill's coverage could not be extended to cover negotiated contracts.

18 *Submission 4*, p. 7.

19 *Submission 11*, p. 4.

20 National Australia Bank, *Submission 30*, p. 4.

together with other terms, the resulting contract comes within the legislative definition of a standard form contract.[21]

Examples of unfair terms

4.27 Section 4 of the bill provides 14 examples of 'the kinds of terms of a consumer contract that may be unfair'. They are:

(c) a term that permits, or has the effect of permitting, one party (but not another party) to avoid or limit performance of the contract;

(d) a term that permits, or has the effect of permitting, one party (but not another party) to terminate the contract;

(e) a term that penalises, or has the effect of penalising, one party (but not another party) for a breach or termination of the contract;

(f) a term that permits, or has the effect of permitting, one party (but not another party) to vary the terms of the contract;

(g) a term that permits, or has the effect of permitting, one party (but not another party) to renew or not renew the contract;

(h) a term that permits, or has the effect of permitting, one party to vary the upfront price payable under the contract without the right of another party to terminate the contract;

(i) a term that permits, or has the effect of permitting, one party unilaterally to vary the characteristics of the goods or services to be supplied, or the interest in land to be sold or granted, under the contract;

(j) a term that permits, or has the effect of permitting, one party unilaterally to determine whether the contract has been breached or to interpret its meaning;

(k) a term that limits, or has the effect of limiting, one party's vicarious liability for its agents;

(l) a term that permits, or has the effect of permitting, one party to assign the contract to the detriment of another party without that other party's consent;

(m) a term that limits, or has the effect of limiting, one party's right to sue another party;

(n) a term that limits, or has the effect of limiting, the evidence one party can adduce in proceedings relating to the contract;

(o) a term that imposes, or has the effect of imposing, the evidential burden on one party in proceedings relating to the contract; and

21 ABACUS, *Submission 33*, p. 7.

(p) a term of a kind, or a term that has an effect of a kind, prescribed by the regulations.

4.28 The EM states that while these examples give statutory guidance on the types of terms which may be regarded as being of concern, 'they do not prohibit the use of those terms, nor do they create a presumption that those terms are unfair'.[22] It is a 'non-exhaustive, indicative' list of the types of terms that may be considered 'unfair'. As the Minister noted in his Second Reading Speech:

> The use of 'grey listed' terms may be reasonable. And any consideration of a 'grey listed' term is subject to the unfair terms test. And, indeed, the consultation paper the government issued on 11 May 2009 acknowledges that businesses may need to do things like assign contracts or vary agreements.[23]

4.29 The EM notes that the examples given in paragraphs (a), (b), (d), (e), (f), (g) and (h) are examples of terms that allow a party to make changes to key elements of a contract on a unilateral basis. However, this does not prohibit unilateral variation terms, not does it create a presumption that these terms are unfair.[24]

4.30 Paragraphs (i), (k), (l), and (m) are examples of types of terms that have the effect of limiting the rights of the party to whom the consumer is presented.

4.31 Paragraph (c) refers to terms that penalise, or have the effect of penalising, one party for a breach or termination of the contract.

4.32 Paragraph (j) refers to terms that allow for a party to assign the contract to the detriment of the other party, without the other party's consent.[25] This example does not prohibit the use of such clauses, however.

Views

4.33 The Consumer Action Law Centre supported the bill's approach of a general definition of an unfair contract in section 3 and an indicative and non-exhaustive list of examples in section 4. It argued that:

> This two-fold approach to defining an unfair term is consistent with the models of successful unfair contract terms laws enacted in other jurisdictions, and reflects best practice in consumer protection regulation by following a "general-plus-specific" model that allows for flexibility to address changing conditions or practices through use of a general definition, but also incorporates clarity and certainty in relation to known

22 *Explanatory Memorandum*, p. 23.

23 The Hon. Dr Craig Emerson, Second Reading Speech, *House of Representatives Hansard*, 24 June 2009, p. 6984.

24 *Explanatory Memorandum*, p. 23.

25 *Explanatory Memorandum*, p. 24.

> current problems as well as guidance in the interpretation of the general provision.[26]

4.34 Some submitters argue that these examples should be taken out of the bill. GE, for example, is concerned that the examples may be misinterpreted as a more proscriptive list. The NAB warned against amending the list of examples by regulation arguing that without due consultation, there will be further uncertainty about what terms are fair and unfair.[27] Similarly, the BCA argued that:

> The inclusion of a list of examples of unfair contract terms is…inappropriate as each of the examples can be interpreted differently and may themselves create a host of new uncertainties. Additionally, as one commentator states, the result of a list approach *"is that normal provisions, appropriate in many circumstances, are at risk of being held to be unfair"*.[28]

'Unconscionable conduct' and 'unfair contract terms'

4.35 The committee discussed the issue of the extent of overlap between the existing provisions relating to 'unconscionable conduct' in the TPA and the provisions of the bill relating to unfair contract terms. The discussion took place in two contexts:

- firstly, the need for the unfair contract terms provisions in the bill to bolster consumer protection, given the lack of protection afforded under the unconscionable conduct provisions; and
- secondly, the extent to which the unfair contract terms provisions in the bill are essentially doubling up on the TPA's unconscionable conduct provisions, and in so doing, creating greater uncertainty for business.

Treasury's view

4.36 Treasury told the committee that the TPA's unconscionable conduct provisions do not relate directly to questions of contract. Rather:

> …they are directed towards matters of conduct, which can encompass the nature of contracts and the way in which contracts are entered into by parties, including businesses.[29]

4.37 Treasury explained that unconscionability might be characterised as a subset of unfairness:

> The concept of unconscionability in the Trade Practices Act relates to the common-law or equitable notion of unconscionability that exists generally,

---

26 Consumer Action Law Centre, *Submission 19*, p. 5.

27 National Australia Bank, *Submission 30*, p. 6.

28 Business Council of Australia, *Submission 20*, p. 4. The BCA was citing George Raitt, 'Unfair contracts bill repeats UK problems', *Australian Financial Review*, 23 July 2009, p. 63.

29 Mr Simon Writer, *Proof Committee Hansard*, 21 August 2009, p. 2.

> and does not seek to define it in any particular way beyond that concept which has been developed by the courts over many centuries, whereas 'unfair contract terms' relates really to a wider consideration of the nature of a term entered into by parties, and the bill sets out a definition of unfairness in this context, which is that there is a significant balance between the parties' rights and obligations arising out of the contract, and the term is not reasonably necessary in order to protect the legitimate interests of the party that would be advantaged by the term. So it does not simply pick up on the general notion of unfairness but seeks to provide some shape to it on the face of the legislation.[30]

The need for unfair contract term provisions

4.38 In expressing their disappointment that the bill does not address business-to-business unfair contract terms (see chapter 5), some submitters drew the committee's attention to the inadequacy of the TPA's unconscionable conduct provisions.

4.39 Associate Professor Zumbo told the committee he doubted whether the government's reviews of the unconscionable conduct provisions of the TPA and the Franchising Code of Conduct would offer an adequate response to protecting small businesses from unfair contract terms. He noted that both reviews focussed on the narrow standard of 'procedural unconscionability'—concerned with conduct surrounding the contract—rather than 'substantive unconscionability', which is solely concerned with the unfairness of the contract terms. Progress on this front, he argued, cannot be considered a substitute for the 'need to deal with the issue of substantive unconscionability through the inclusion of small businesses in the unfair contract terms'.[31]

4.40 In this context, Associate Professor Zumbo supported section 3(1) of the bill and rejected any claim that this basis for defining 'unfair' is nebulous.[32] He told the committee that in the bill:

> We have a definition of what is unfair, which is a significant imbalance between the rights and obligations of the parties, and we have the term 'not reasonably necessary to protect' big business. That becomes the focal point and the fact that you define it in those terms removes all the elements of doubt that that there may be as to what unfairness may mean if you simply say, 'You shall not engage in unfair conduct'. This definition of unfairness in the unfair contract terms regime is a test that sort of mirrors the Victorian test and the UK test and it works well in those jurisdictions.[33]

4.41 Mr Delaney of the MTAA told the committee that:

---

30 Mr Simon Writer, *Proof Committee Hansard*, 21 August 2009, p. 2.

31 Associate Professor Frank Zumbo, *Submission 12*, p. 5.

32 As chapter 6 notes, Associate Professor Zumbo does have difficulty with the bill's 'detriment' and 'transparency' tests in subsections 3(2) and 3(3).

33 Associate Professor Frank Zumbo, *Proof Committee Hansard*, 26 August 2009, p. 31.

> The unconscionable conduct provisions have been entirely disappointing, and that is why the government is looking at them. It was an election undertaking, which we were grateful for. Mr Samuel sees it somewhat differently—that over the 10 years or so that they have been in the act the commission has taken every effort to pursue them. There have been a couple of what were thought to be landmark cases, but they have subsequently been entirely confined to circumstances that have not been replicated otherwise. To be fair, there has been some behaviour change, but what the parliament thought it would secure by those changes has just not appeared.[34]

4.42 Ms Ann Dalton of the Pharmacy Guild argued that:

> …the protection offered by the unconscionable conduct provisions currently contained in the Trade Practices Act are illusory, and for that reason was pleased that the Australian Consumer Law at least proposed to cover unfair standard form business-to-business contracts when it was first circulated. Like many other small business groups, such as the Motor Trades Association of Australia, the guild is disappointed that the provision was removed at the last moment. The guild supports the view of the non-government senators expressed in the Birdsville amendments inquiry conducted by this committee, in which they called for the Victorian legislative framework for consumer transactions to be extended to cover business-to-business relationships involving small business.[35]

4.43 The Pharmacy Guild recommended removing the unconscionable conduct provisions of the TPA and framing the Australian Consumer Law 'in a manner similar to section 12 of the Independent Contractors Act'. This section permits reviews of contracts that are generally unfair or harsh and uses the term 'unfair' without any statutory extension.[36]

4.44 Mr Kerry Corke, a consultant to the Pharmacy Guild, told the committee that the concept of unconscionable conduct:

> …as a New South Wales Court of Appeal case called World Best Holdings, discussed in our submission, notes, the concept of what is unfair and what is unconscionable 'overlaps but is not quite the same'. The term 'unfair' is generally taken by that case law to be a lower threshold than unconscionability.[37]

4.45 Mr Corke referred to the case of *Keldote Pty Ltd v Riteway Transport*, the first case of the Federal Magistrates Court that considered the concept of unfair contract in the field of independent contractors. He noted that in this case:

---

34 Mr Michael Delaney, *Proof Committee Hansard*, 21 August 2009, p. 20.

35 Ms Ann Dalton, *Proof Committee Hansard*, 21 August 2009, p. 13.

36 Mr Kerry Corke, *Proof Committee Hansard*, 21 August 2009, p. 14.

37 Mr Kerry Corke, *Proof Committee Hansard*, 21 August 2009, p. 14.

> …the test of unfairness involves the common sense approach characteristic of the ordinary jury member by applying standards providing a proper balance or division of advantage or disadvantage between the parties who have made the contract.
>
> We think that probably puts best the reason why a concept of unfairness as a threshold to review an unfair contract is preferable to the higher threshold of unconscionable conduct, although it has to be said at the end of the day it all is a question of fact and degree.[38]

4.46 The Insurance Law Service gave first-hand evidence of the need for a lower threshold than the current unconscionable conduct provisions in the TPA. Ms Katherine Lane gave the example of standard form banking contract relating to fixed rates:

> One person rang up the bank and said, 'I'll fix my rate' and they did not even get consent from the other partner. When the other person said, 'Why were they allowed to fix the rate without my consent?' they were told: 'We've changed the terms of the contract on the unilateral change clause.'…
>
> Unfortunately, for the last many years, even though we have unconscionable conduct provisions and all of that, they have not worked for this type of problem. If I went to court I would lose if I was arguing unfair term. I have been unable to do anything with them and so I have had to advise consumer after consumer after consumer that yes, it is unfair—in fact, this is one of my mantras. I say, 'Yes, that's unfair, but can we do anything about it legally? No. But, by the way, they're talking about bringing in legislation.' I receive lots of calls where people say, 'This is unfair.' Whether it will be or not when we look at it in the light of day is a different story—but do I get thousands of calls from consumers saying things are unfair?[39]

38 Mr Kerry Corke, *Proof Committee Hansard*, 21 August 2009, p. 16.

39 Ms Katherine Lane, *Proof Committee Hansard*, 26 August 2009, p. 48.