

Chapter 2

'Unconscionable conduct' and the Trade Practices Act

'Unconscionable conduct' as currently codified in the TPA

2.1 Currently, there are three separate subsections of Part IVA of the *Trade Practices Act 1974* that deal with 'unconscionable conduct'; 51AA, 51AB and 51AC. Section 51AA deals with 'procedural unconscionability' which relates to the formation of a contract; sections 51AB and 51AC deal with 'substantive unconscionability' which relates to the actual operation of a contract.

2.2 Introduced in 1992, subsection 51AA states that 'a corporation must not, in trade or commerce, engage in conduct that is unconscionable within the meaning of the unwritten law, from time to time, of the States and Territories'. 'Unwritten law' refers to the law developed by the courts of common law and equity. The reference to unconscionability in section 51AA stems from the traditional equitable doctrine of unconscionability relating to unconscionable bargains and special disadvantage.¹

2.3 The equitable doctrine of unconscionability was expounded by Justice Mason in *Commercial Bank of Australia Ltd v Amadio* (1983) who referred to 'special disadvantage' as:

...the class of case in which a party makes unconscientious use of his superior position or bargaining power to the detriment of a party who suffers from special disability or is placed in some special situation of disadvantage, e.g., a catching bargain with an expectant heir or an unfair contract made by taking advantage of a person who is seriously affected by intoxicating drink.²

2.4 Significantly, the High Court made clear that a mere disparity in bargaining power between the two parties would not, in itself, be considered a 'special disability'. One of the parties must be affected in their ability to make a judgment as to his or her own best interests. The *Amadio* judgment also established that it is only the setting in which a contract is made that is relevant to a finding of unconscionability: if the *operation* of the contract is harsh, it cannot be impeached on the grounds of unconscionability.³

1 See paragraph 1.3

2 (1983) 151 CLR 447 at 461.

3 Liam Brown, 'The impact of section 51AC of the Trade Practices Act 1974 (Cth) on commercial certainty', *Melbourne University Law Review*, vol 28, 2004, p. 595.

2.5 Subsection 51AB was the original provision in the TPA on 'unconscionable' conduct. It was first inserted in section 52 of the Act in 1986⁴ but was shifted to section 51AB as part of the 1992 amendments.⁵ Subsection 51AB(1) states that 'a corporation shall not, in trade or commerce, in connection with the supply or possible supply of goods or services to a person, engage in conduct that is, in all the circumstances, unconscionable'. Subsection 51AB(2) states the matters to which a court may have regard in determining whether a corporation has contravened subsection 1. These include:

- the relative strengths of the bargaining positions of the corporation and the consumer;
- whether the consumer was required to comply with the conditions that were not reasonably necessary for the protection of the legitimate interests of the corporation;
- whether the consumer was able to understand any documents relating to supply of the goods or services;
- whether any undue influence or pressure was exerted on, or any unfair tactics were used against, the consumer or a person acting on behalf of the corporation in relation to the supply of goods or services; and
- the amount for which the consumer could have acquired identical or equivalent goods or services from a person other than the corporation.

2.6 Section 51AC was introduced in 1998 to protect small business from unconscionable conduct.⁶ Similar to s51AB(2), subsections s51AC(3) and 51AC(4) list a number of factors that the courts may consider in determining whether the conduct of the 'supplier' (51AC(3)) or the 'acquirer' (51AC(4)) is unconscionable (*without in any way limiting the matters to which the Court may have regard*). These include the five factors listed in section 51AB(2) (above) in addition to the following factors:

- the consistency of the conduct with similar transactions;
- the requirements of any applicable industry code;
- the non-disclosure of conduct which might affect the person's interest;
- the extent of negotiation of a contract;
- whether the supplier / acquirer has a contractual right to vary unilaterally a term or condition of a contract; and

4 *Trade Practices Revision Act 1986*, No. 17

5 *Trade Practices Legislation Amendment Act 1992*, No. 222

6 The amendment was based on a recommendation by the House of Representatives Standing Committee on Industry, Science and Technology in its May 1997 report into fair trading: *Finding a Balance: Towards Fair Trading in Australia* (also known as the 'Reid Report').

- the extent to which the parties acted in good faith.

2.7 Some argue that these factors make section 51AC work well. Mr Liam Brown, a Victorian lawyer formerly with Mallesons Stephen Jaques, has argued that the eleven factors listed in the section contain both procedural and substantive elements which allow the courts to look at both bargaining practices and outcomes. He thereby claimed that section 51AC is a 'workable approach' to prevention of unconscionable conduct; broader than section 51AA and better defined than section 51AB.⁷

2.8 Others argue that the factors in 51AC(3) and 51AC(4) are of limited practical use. They can be considered or dismissed at the court's discretion and they do not define 'unconscionable conduct'. The court determines whether or not the conduct in question is unconscionable based on the circumstances of the case, whether these are listed in section 51AC(3) or not.⁸

Case law and section 51AC

2.9 As mentioned above, 'unconscionable conduct' is not defined in section 51AC. The courts are heavily reliant on case law to guide their decisions on this section. Three cases are of particular note.

Australian Competition and Consumer Commission v Simply No-Knead (2000)

2.10 The case involved a dispute between Simply No-Knead (SNK) and a number of its franchisees. The franchisees complained that SNK had withheld orders of supplies in order to press them into complying with its demands. In addition, SNK had refused to negotiate, refused to provide disclosure documents as required by the Franchising Code, and had distributed promotional material which excluded the franchisees' names.

2.11 This case was one of only two successful ACCC-initiated section 51AC prosecutions. It was a clear case of substantive unconscionability, where the post-contractual conduct of the defendant was 'simply so bad' that it met the threshold requirement. As Justice Sundberg concluded:

I have concluded that the accumulation of incidents...discloses an overwhelming case of unreasonable, unfair, bullying and thuggish behaviour in relation to each franchisee that amounts to unconscionable conduct by SNK for the purposes of s 51AC(1)...SNK's conduct achieved its aim. Between August and November all the franchisees either

7 Liam Brown, 'The impact of section 51AC of the Trade Practices Act 1974 (Cth) on commercial certainty', *Melbourne University Law Review*, vol 28, 2004, p. 600.

8 Associate Professor Zumbo, *Submission 11*, p. 15.

terminated their agreements or did not renew them. There is no doubt that SNK's conduct was a cause of their respective decisions in this regard.⁹

*Garry Rogers Motors (Australia) Pty Ltd v Subaru (Australia) Pty Ltd (1999)*¹⁰

2.12 In 1997, Subaru introduced its 'six star' programme of service enhancement. Garry Rogers Motors, an authorised Subaru dealer since 1991, advised that it was unwilling to comply with all parts of the programme. Subaru subsequently gave notice of termination of the agreement. Despite Garry Rogers' repeated attempts to show that it had changed its mind and was prepared to comply with the programme, Subaru refused to revoke the notice. Garry Rogers alleged that the termination of the dealership constituted unconscionable conduct.

2.13 The court refused to give relief 'simply for harsh contractual terms when the circumstances of the case indicate that the defendant has not behaved in a particularly reprehensible way either during contractual formation or performance'. The judge ruled that the behaviour of Subaru lacked the necessary threshold requirement of section 51AC; namely, that the conduct complained of was, *in all the circumstances*, unconscionable. There had been no procedural unconscionability and Subaru had merely acted to protect its commercial interest.¹¹

*Hurley v McDonald's Australia (2000)*¹²

2.14 The restaurant chain, McDonald's, ran a promotional game which required participants to collect tokens in a particular sequence to qualify for particular prizes. Ms Hurley claimed a prize based on a mixture of tokens from the previous and current years.

2.15 McDonald's relied on a condition of entry clause to reject Ms Hurley's claim. Ms Hurley argued that McDonald's had acted unconscionably in breach of s51AB. The court noted that the common feature of ss51AB and 51AC was that they required a demonstration of 'serious misconduct or something clearly unfair or unreasonable' beyond the terms of the contract. In this case, McDonald's rejection of the claim was not considered to be particularly harsh or unreasonable in the circumstances.

2.16 The ruling has elicited different reactions. Mr Liam Brown noted that this ruling prevented plaintiffs from using section 51AC 'simply to complain about a

9 Simply No-Knead and Cameron Bates [2000] FCA 1365, [51]; ACCC News Release dated 25 September 2000, <www.accc.gov.au.>

10 (1999) 21 ATPR

11 Liam Brown, 'The impact of section 51AC of the Trade Practices Act 1974 (Cth) on commercial certainty', *Melbourne University Law Review*, vol 28, 2004, p. 614.

12 (2000) 22 ATPR

contract that is harsh in its operation'.¹³ Associate Professor Zumbo has described this ruling as the 'final nail in the coffin' for section 51AC.¹⁴

2.17 Case law therefore establishes 'serious misconduct' as the threshold for a finding of unconscionable conduct. It is not adequate for a small business plaintiff to cite conduct contrary to one (or various) of the factors listed in 51AC.¹⁵ There must be evidence of procedural misbehaviour in contract formation or an absence of 'good faith'.¹⁶ There is an important issue, however, as to whether the courts and the regulator have been overly cautious in developing section 51AC case law.

The legal view of 'unconscionability'

2.18 Several commentators have noted that the 'unconscionable conduct' provisions in Australian law are very case-specific. Justice Paul Finn has noted that while there are unconscionable conduct provisions in the TPA, the *Corporations Act 2001* and the *Australian Securities and Investments Commission Act 2001* (section 12CA–12CC):

The one thing we can say with confidence is that it does not have a uniform meaning in the various sections it inhabits.¹⁷

2.19 In similar vein, Professor Bryan Horrigan has observed:

Unconscionability may be considered a "descriptive theme" for the grouping together of various strands of doctrine, but the theme itself cannot be used as some kind of overarching test.¹⁸

2.20 In a 2007 article, James Davidson explained this issue in the following way:

The use of the umbrella term 'unconscionable' is convenient but then to try and fit circumstances into the doctrine on the basis that they seem 'unconscionable' or 'unfair' within the popular meaning of those words would be to misunderstand the applicability of the doctrine. Put simply, the logic is that a set of circumstances between two parties which give rise to relief under the doctrine of unconscionability may also be the circumstances which are unfair and unconscionable in the popular sense of the word, but

13 Liam Brown, 'The impact of section 51AC of the Trade Practices Act 1974 (Cth) on commercial certainty', *Melbourne University Law Review*, vol 28, 2004, p. 616.

14 Associate Professor Zumbo, *Proof Committee Hansard*, 3 November 2008, p. 4.

15 This is what Liam Brown has referred to as the 'scattergun' approach. He notes that it is not surprising that these cases have rarely succeeded. 'The impact of section 51AC of the Trade Practices Act 1974 (Cth) on commercial certainty', *Melbourne University Law Review*, vol 28, 2004, p. 613.

16 Liam Brown, 'The impact of section 51AC of the Trade Practices Act 1974 (Cth) on commercial certainty', *Melbourne University Law Review*, vol 28, 2004, p. 621.

17 Justice Paul Finn, 'Unconscionable conduct?', *UNISA Trade Practices Workshop – 2006*

18 Professor Bryan Horrigan, 'The expansion of fairness-based business regulation', *Australian Business Law Review*, vol 32, 2004, p. 169.

popularly held precepts of unfairness or unconscionability will not on their own invoke the doctrine.¹⁹

2.21 Indeed, in their submission to this inquiry, the ACCC emphasised that what is 'unconscionable' will depend on the facts of the case and the particular circumstances in which the conduct occurs. In other words, 'the same conduct may be characterised differently depending on the circumstances in which it occurs'.²⁰

The structure of the report

2.22 The crux of this inquiry is whether or not section 51AC of the TPA is working according to its legislative intent. There are two broad views.

2.23 The first is that the development of case law on section 51AC has been disappointing and that the section is therefore not working. In other words, there are many more unfair contract terms ('substantive unconscionability') operating in Australia than what the prosecution record would indicate. Accordingly, the courts need greater guidance in interpreting the Act which could be achieved through a definition or examples of 'unconscionable conduct'. Chapter 3 of this report examines these views.

2.24 The opposing view is that section 51AC has worked, and is working well. The lack of successful prosecutions is evidence that business is complying with the law. Any amendment to section 51AC of the TPA would create uncertainty, confusion and less flexibility for the courts to adjudicate on 'unconscionable conduct' cases. Chapter 4 of this report examines this argument.

2.25 Chapter 5 presents the committee's view on the need to amend section 51AC of the TPA and the scope and content of these amendments.

19 James Davidson, 'Unfair contract terms and the consumer: A case for proactive regulation?', *Competition and Consumer Law Journal*, vol. 15, No. 1, August 2007, pp. 74–92.

20 Australian Competition and Consumer Commission, *Submission 27*, p. 2.