

## Unfair contract provisions to protect small businesses

9 November 2016

From 12 November 2016, unfair terms in standard form contracts with small businesses may be declared void. Special Counsel, Nicola Nygh, discusses the extension of the protection currently available to consumers under the *Australian Consumer Law* (the **ACL**) and the *Australian Securities and Investments Commission Act* (the **ASIC Act**).

If a court or tribunal finds that a contractual term is unfair, the term will be declared void. The rest of the contract will be binding on the parties only to the extent that the contract can operate without the unfair term. If they have not already done so, businesses that contract with small businesses should review their standard form contracts to ensure that they do not contain unfair terms within the meaning of the ACL. Small businesses should be aware of their increased rights in respect of contracts entered into, renewed or varied from 12 November 2016.

### Contracts affected

The new laws apply to contracts entered into or renewed by small businesses on or after 12 November 2016. The laws will also apply to terms of existing contracts where those terms are varied on, or after, 12 November 2016.

Contracts affected by the laws are standard form contracts for the supply of goods or services or the grant of an interest in land where:

- the contract has been prepared by one party and the other party has little or no opportunity to negotiate the terms;
- at least one party is a business that employs less than 20 people; and
- the upfront price payable under the contract is no more than \$300,000 or \$1 million if the contract is for more than 12 months.

The upfront price includes any payments for the supply or grant that are clearly disclosed at the time the contract is entered into. However, it does not include payments that are not quantifiable at the time the contract is entered into, such as commissions or royalties that are calculated as a percentage of sales.

### Meaning of unfair

A term will be unfair under the ACL or ASIC Act if it:

- causes significant imbalance between the parties' rights and obligations;
- is not reasonably necessary to protect the legitimate interests of the party advantaged by the term; and
- would cause significant detriment (such as delay) to the small business if it were relied upon.

In determining whether a term is unfair, a court must consider both how transparent the term is and the overall rights and obligations of each party to the contract. Thus, whether a term is unfair must be considered in the context of the whole contract and a term, that is potentially unfair to one party, may be counter balanced by other terms, that give an advantage to the other party.

The following terms are excluded from the law and cannot be found to be unfair:

- terms that define the main subject matter of the contract;
- terms that set the upfront price payable; and
- terms that are required or expressly permitted by Federal or State law.

### **Examples of unfair terms**

Fourteen examples of terms that may potentially be unfair are set out in s25 of the ACL. The examples *provide 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.*<sup>1</sup> Broadly, the examples are terms that give unilateral rights to, or impose unilateral obligations on, one party such as terms that:

- allow only one party to avoid or limit its obligations under the contract;
- allow only one party to terminate, or alternatively to renew, the contract;
- penalise only one party for breaching or terminating the contract; or
- allow only one party to vary the terms of the contract.

### **Industries in which unfair contract provisions may apply**

The provisions in the ACL are not limited to any particular industries. However, some guidance as to the contexts in which the ACCC expects that the new law may apply can be gleaned from the fact that in the 12 months prior to the new law coming into effect, the ACCC has been monitoring the following industries:

- franchising;
- retail leasing;
- advertising services;
- telecommunications services; and
- independent contracting (e.g. IT consultants and architects).

The provisions in the ASIC Act will apply to contracts with small businesses for financial products and services including business loans, credit cards and client or broker agreements.

### **Conclusion**

The new laws attempt to balance the efficiencies that flow from standard form contracts to both the economy as a whole and to small businesses in particular with the potential for standard form contracts to unfairly advantage the party that prepared the contract at the expense of the other party. To achieve this, the legislation requires the court to make a value judgment as to whether a term is unfair in the context of the entire contract, while paying close attention to the guidance in the statute. In determining what is unfair, some guidance can also be obtained from Chief Justice Allsop's observation that *unjustness and unfairness are of a lower moral or ethical standard than unconscionability.*<sup>2</sup>

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<sup>1</sup> Explanatory Memorandum to the *Trade Practices Amendment (Australian Consumer Law Bill (No 2) 2010 (Cth)* at [5.44].

<sup>2</sup> *Paciocco v Australia and New Zealand Banking Group Limited* [2015] FCAFC 50 at [363].