

29 May 2009

The Hon. Chris Bowen MP
Assistant Treasurer
Minister for Competition Policy and Consumer Affairs
Parliament House
CANBERRA ACT 2600

Business
Council of
Australia

By email: chris.bowen.mp@aph.gov.au



Dear Minister

NATIONAL UNFAIR CONTRACT TERMS

The Business Council of Australia (BCA) writes to you regarding the exposure draft of the National Unfair Contracts Provisions released on 11 May 2009.

The BCA represents the chief executives of over 100 of Australia's leading companies. The BCA develops and advocates, on behalf of its members, public policy reform that positions Australia as a strong and vibrant economy and society. The businesses that the BCA Members represent characterise a substantial share of Australia's domestic and export activity.

The BCA supports the reform of the consumer protection laws in Australia, and in particular the development of a nationally consistent approach. However, the BCA believes that these draft provisions represent a significant departure from previous considerations of a national consumer law framework as well as from models adopted elsewhere in Australia and overseas. The BCA considers that the proposals as currently drafted, represent a substantial change to the fundamental underlying principles of contract law and present a significant risk for Australian businesses across all sectors.

A key contributor to the continuing success of the Australian economy is effective competition laws. These laws should support vigorous competition as a means of driving productivity, efficient markets and lower prices for consumers. Through the course of their normal operations, businesses should not be hampered by the imposition of unnecessary and inappropriate additional costs in business-to-business transactions. We are concerned that this proposal will stifle ordinary business activities.

The BCA strongly believes that regulatory intervention should only occur where there is a clearly identifiable problem to be addressed and where the costs of the regulation do not outweigh the benefits. Unnecessary costs should not be imposed on business. Any amendments that may stifle ordinary and legitimate commercial conduct or competition should therefore be avoided.

With this in mind, it is imperative that any new business laws or proposed changes to existing laws must be subject to a proper economic analysis in conjunction with timely, comprehensive and meaningful consultation with business.

The BCA is particularly concerned that these proposals directly contradict commitments made by the government to pursue proper regulatory process and evidenced based policy development. Moreover the BCA is concerned at the short timeframe provided for submissions as well as the proposed introduction of regulations into Parliament.

Comprehensive consultation and collection of evidence

The BCA considers that the short timeframe for consultation and implementation of this significant law fundamentally undermines any effective regulation making process. As Gary Banks stated in his speech on evidenced-based policy making:¹

There is an obvious clash between any government's acceptance of the need for good evidence and the political 'need for speed'. But the facts are that detailed research, involving data gathering and the testing of evidence, can't be done overnight.

The BCA is deeply concerned that only nine business days (less than two weeks) have been allowed for this round of consultation. Previous consultations in relation to these laws assumed a scope of application consistent with unfair contracts laws in major overseas jurisdictions and elsewhere in Australia. The short timeframe for responses is particularly concerning therefore, given the significant changes to fundamental contractual principles represented in these draft provisions. Such a significant proposal is one which deserves considered attention and warrants a cautious approach.

In addition, the BCA is concerned about the consideration that the government is able to afford submissions, and the absence in the timetable of a further round of consultations, if necessary, in advance of the stated introduction of legislation into Parliament in the winter sitting in June 2009.

Evidence-based policy development – lack of demonstrated problem at which proposals are aimed

The government has committed to using an 'evidence based' policy development approach. In an address to senior public servants in April last year, the Prime Minister observed that, "*evidence-based policy making is at the heart of being a reformist government*".²

Accordingly, proposed changes to existing laws should only occur where there is a clearly evidenced market problem to be addressed. In the BCA's opinion not enough evidence has been provided to justify the scope of these laws being extended to business-to-business standard form contracts.

¹ Gary Banks Chairman Productivity Commission, *Evidence-Based Policy-Making: What is it? How do we get it?*, ANZSOG/ANU Public Lecture Series 2009, Canberra, 4 February, p 15

² Gary Banks, Chairman Productivity Commission, *Evidence-Based Policy-Making: What is it? How do we get it?*, ANZSOG/ANU Public Lecture Series 2009, Canberra, 4 Feb, p 3

The media release dated 11 May 2009 states that:³

“This new provision will give all Australian consumers access to protection from unfair contract terms in standard-form contracts.

Under the Rudd Government’s national unfair contracts terms provision, action will be able to be taken against ‘unfair’ terms in standard-form contracts by individual consumers, small business or Commonwealth or State consumer protection agencies.”

The proposals outlined in the consultation paper go beyond the objectives outlined in your Media Release and seek to capture standard form contractual arrangements not only in relation to individual consumers and small businesses, but also standard form contracts between all businesses (including large businesses) in all sectors of the economy.

The government has not demonstrated an economic market failure across the Australian economy that requires the extension of the definition of ‘consumer’ to cover business-to-business standard form contracts.

In articulating its objectives, the government indicated its intention that provisions will *“apply to business-to-business transactions in the same way as other key provisions in the TPA do, such as those dealing with unconscionable conduct and misleading and deceptive conduct”*⁴. However, it is not clear that including large businesses in the context of unfair contract provisions is consistent with those key competition laws. For example section 51AC, dealing with unconscionability in business transactions, excludes listed public companies.

The aim of these provisions is to protect those consumers that are less able to bargain in relation to ‘take it or leave it’ contracts, ‘whether they are ordinary people, institutions or businesses.’⁵ There is no evidence that large businesses being party to standard form business-to-business contracts require such protection. Large businesses are generally sufficiently resourced and should have little need to argue that terms of their contractual arrangements are void on the basis of unfairness.

It is also unclear how the new laws will affect small businesses. Small businesses also deal with big businesses and consumers under standard form contracts, and will use standard form contracts to minimise unnecessary and inefficient transactions costs.

³ Media Release No. 039, 11 May 2009

⁴ The Treasury, *The Australian Consumer Law*, Consultation Paper, 11 May 2009, p 8

⁵ The Treasury, *The Australian Consumer Law*, Consultation Paper, 11 May 2009, p iii

'Cost-benefit' analysis

Another feature of good regulatory process is that proposed reforms should achieve the purpose for which they are intended and should not be disproportionate or stifle ordinary and legitimate business behaviour. Gary Banks stated the following in his speech on evidence-based policy development:⁶

Most evidence-based methodologies fit broadly within a cost-benefit (or at least cost effectiveness) framework, designed to determine an estimated (net) payoff to society. It is a robust framework that provides for explicit recognition of costs and benefits, and requires the policy maker to consider the full range of potential impacts.

It is essential to strike a balance between assisting or protecting consumers and ensuring that undue burdens are not imposed on business and the economy. As the Productivity Commission stated in its review of the consumer policy framework:⁷

".....consumer policies that help consumers in one facet of their dealings with business, may create compliance burdens or dull incentives for productivity improvement, which then rebound on consumers through increased prices or as reduced incomes..."

Standard form contracts are essential to business operations, through the cost savings and efficiencies they provide. However, the scope of the draft unfair contract provisions applies to business-to-business standard form contractual arrangements and may therefore increase costs and reduce efficiencies. For example:

- The new provisions, if enacted, will require all businesses to review all of their existing standard-form contractual arrangements and prepare new documents.
- A significant concern is Division 2 of the proposals which create an unqualified power to ban certain kinds of contractual terms through the use of regulations. This means that certain contractual terms could be banned in the future without legislative processes, cost-benefit analysis or consultation with the public (including business). This may impose significant additional risks and costs to business. For example, businesses may have to review and re-draft all of their existing standard form contracts each time the regulations are amended. The prohibition of certain terms by means of regulation without appropriate legislative debate is of significant concern and is clearly counter to proper legislative and policy process.
- Standard form contractual arrangements have enabled businesses to have a degree of certainty with respect to their rights and obligations and ability to enforce contractual terms. The proposed provisions introduce uncertainty of enforcement leading to greater risks for contracting parties. The new provisions are likely to require businesses to re-allocate contract risks and reprice their goods and services.

⁶ Gary Banks Chairman Productivity Commission, *Evidence-Based Policy-Making: What is it? How do we get it?*, ANZSOG/ANU Public Lecture Series 2009, Canberra, 4 February, p 10

⁷ Productivity Commission 2008, *Review of Australia's Consumer Policy Framework*, Final Report, Canberra, p 4

- Standard form contracts avoid extensive and costly negotiations and therefore increase efficiency. The government claims that many contractual arrangements would not fall within the ambit of the new unfair contract provisions if they are negotiated. The effect of the new unfair contract laws is to incentivise parties to partake in costly and drawn-out negotiation.
- Standard form contractual arrangements reduce administrative burdens, such as reduced staff training needs. Expertly trained staff will be required to deal with contractual arrangements if there is a propensity towards non-uniform contractual arrangements.
- These draft provisions are likely to discourage investment not only domestically but also from overseas. Investment into Australia may be discouraged, where overseas businesses fear that contractual arrangements entered into in Australia are uncertain or risky. The proposed laws go beyond models introduced in any countries overseas. The Consultation Paper refers to the unfair contracts terms that exist in the UK and the EU⁸. In those jurisdictions the operation of unfair contract provisions are generally limited, for example to people not acting in a business or professional capacity.

A thorough cost-benefit analysis on the impacts of these proposed new laws on standard form contracts across the Australian economy is required. Given the prevalence of standard form business-to-business contracting across the economy, the BCA considers that this law will create a significant increase in costs for business. Whilst enough time hasn't been given to determine the economy-wide costs of this proposal on business, one BCA Member indicated that:

Virtually all of its customer contracts are business-to-business and a substantial majority of those are likely to be considered to be with small businesses. Around 80% of its contracts are in standard form. Therefore, the impact of this legislation on its business would be substantial.

Ordinary business transactions will become infused with greater risks than was the case previously. This will ultimately translate into higher prices for consumers. This concern has been expressed by a broad range of stakeholders in the community including business, academics and lawyers. For example one lawyer commented:⁹

The whole notion of big corporates being able to rely on their contractual terms with certainty is no more, and they've got to factor in the cost of that risk – and that will inevitably flow through to prices. In these economic times, when we're supposed to be assisting businesses and boosting productivity, to have this sort of business cost imposed across the board is outrageous.

⁸ The Treasury, *The Australian Consumer Law*, Consultation Paper, 11 May 2009, p iii

⁹ Ashley Midalia, 'Contract terms a B2B hazard', *The Australian Financial Review*, 18 May 2009, p 9

Specific issues

The BCA has concerns with a number of areas of the draft provisions, and in particular the introduction of new concepts and terms which add uncertainty to the operation of the laws. The draft laws in many respects go well beyond the recommendations of the Productivity Commission review. For example, some of the high level issues of concern are as follows:

- The definition of a 'standard form' contract is unclear – how much negotiation is required to take a contract outside the scope of the unfair contract provisions? On one interpretation it would be necessary to negotiate every term.
- The proposed definition of what amounts to an 'unfair' contract term does not require that a detriment actually be demonstrated. Instead, the definition will cover contract terms that only 'theoretically' could be considered 'unfair'. This directly contrasts with the recommendations of the Productivity Commission in its review of consumer laws.
- Care must be taken in introducing new concepts and definitions into the competition laws, which have the risk of introducing new uncertainty. There is a need to review the operation and effect of some of the proposed definitions. For example:
 - it is common for parties to contracts generally, to have unequal bargaining power to varying degrees. Determining what is meant by 'unfair' may therefore be quite difficult to ascertain. One party may for example accept a standard form contract term that they may not normally have accepted, in order to gain another sort of advantage, such as speed in the process or an acceptable price. It is unclear how the contractual arrangement and any trade-offs (such as speed or price) are to be taken into consideration. Further review should be given to what the court could take into account in determining whether a term of a standard form contract is 'unfair'. Additionally, it should be made clear that the circumstances being considered are those prevailing when the contract was entered into rather than when the parties are in dispute.
 - in determining whether a term of a contract could be considered to be 'unfair', the draft provisions provide that the court can consider the 'extent to which the term is transparent'. The concept of 'transparency' is uncertain and parties to contracts may find it difficult to know exactly how to comply with the test of 'transparency'. Does this involve font size, written explanatory materials or other specific explanations?
- Including 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.
- The draft proposals provide that, in the event that a term is found unfair, "[t]he contract continues to bind the parties if it is capable of operating without the unfair term". This moves the law beyond the common law test of severability. Accordingly this should be deleted from the proposals, and the existing common law test of severability should continue to apply.

- The draft proposals reverse the onus of proof, such that the party relying on the term needs to show that the term was reasonably necessary to protect its legitimate business interests. This represents a significant departure from traditional standards of proof in contractual proceedings and therefore requires further consideration, including cost-benefit analysis, in order to establish whether a case exists for such a reversal. The application of such a reversal in the context of business-to-business transactions is particularly unusual and highlights the inappropriateness of the broad application of this proposed law.

Way forward

The BCA considers that a cautious approach should be taken to the introduction of unfair contracts law to avoid the introduction of unnecessary new laws that will have the effect of imposing significant new costs and create business uncertainty. Further work is required on the proposals to create a national consumer law, both to assess their practical implications and economic impact more broadly.

In light of these issues and concerns, the BCA considers that:

- If the government is able to demonstrate that there is a market failure in respect of business-to-business standard form contractual arrangements, then a new Productivity Commission review would be warranted. Genuine consideration should be given to those areas that could be dealt with through non-regulatory methods (such as guidance); and
- following the Productivity Commission review, a revised exposure draft of legislation and draft guidance should be released for public consultation, with an appropriate time frame given for public responses and for consideration of the responses.

I have copied this letter and submission to the Treasurer, Wayne Swan MP, the Minister for Finance and Deregulation, Lindsay Tanner MP and the Minister for Small Business, Independent Contractors and the Service Economy; Minister Assisting the Finance Minister on Deregulation, Dr Craig Emerson MP for their information.

Please feel free to contact me or Leanne Edwards, Assistant Director – Regulatory Affairs on (03) 8664 2614 or leanne.edwards@bca.com.au, should you require any additional information or input.

Yours sincerely



Katie Lahey
Chief Executive

cc. The Hon. Wayne Swan MP
The Hon. Lindsay Tanner MP
The Hon. Dr Craig Emerson MP