

Unfair Contract Terms part 2: Strengthening the unfair term laws by making several key changes – What do those changes mean for your small business?

Background

In addition to last week's Part 1, Unfair Contract Term bulletin, we now dive into the unfair term laws and what those changes mean for your small business.

When operating a business, it is your **duty** to have **knowledge of your rights** and enforce them. Currently, unfair contract terms (UCTs) are not unlawful and can only be void when they are found. These terms are sometimes hidden within contracts and you may not even realise that they are unfair. However, on 10 November 2020, the Federal Government announced that it planned to amend the UCT regime to make UCTs, *unlawful* (rather than merely void) and empower the courts to impose a monetary penalty. Although, courts are to be given the power to issue civil penalties for breaches of unfair term laws, there has been no announcement as to how these penalties are to be calculated. More information from VACC on this will be provided once available.

What makes a contract term unfair?

A term in a standard form small business contract is 'unfair' if the following **elements** are satisfied:

1. would cause a **significant imbalance in the parties' rights and obligations** arising under the contract
2. is **not reasonably necessary to protect the legitimate interests** of the party that would benefit from the term, or
3. would **cause detriment** (financial or otherwise) to a small business if it were to be applied or relied on.

Key Change No.1

The onus is on the plaintiff to prove elements (1) and (3) but the onus is on the defendant to disprove item (2) above. This is significant because the validity of an indemnity or a limitation of liability clause may turn on whether the defendant can prove it was reasonably necessary to protect one of its legitimate interests.

Only a court can **make a determination** that a contract term is unfair. This is a major extension of the UCT laws' reach, as it makes common forms of insurance, such as car insurance, house and contents insurance, travel insurance and life insurance, subject to the UCT laws.

In addition, when determining whether a term is unfair, a court must also consider whether the term is **"transparent"**. A term is transparent if it is expressed in reasonably plain language, legible, presented clearly and readily available.

The UCT laws contain a list of terms which *may* (not must) be unfair. This is colloquially called the "grey list". It includes terms that limit, or have the effect of limiting, one party's right to sue another party or one party's vicarious liability for its agents. These terms are clearly relevant to limitations of liability. There is no term in the grey list which expressly refers to indemnities.

Key Change No.2

The UCT regime would plainly render void any term, in a car insurance contract, that entitled an insurer to cash settle the insured's claim for an amount that did not reflect the **true cost of repair**. The fair and reasonable cost of repairs must be paid on the claim (to the insured or the insured's nominated repairer) for the amount the insured **would incur to repair their vehicle**.

This means, that in a car insurance contract which entitles an insurer to pay a **cash settlement to the insured**, rather than repair the vehicle by sending an authority to the repairer chosen by the insured, **may** be considered unfair if it allows the insurer to offer an amount that is **less than** what it would actually cost the insured with their repairer to have the car repaired.

Key Change No.3

The definition of small business will be expanded from less than 20 employees to less than 100 employees and an annual turnover test of less than \$10 million will be introduced as an alternative threshold for determining eligibility (including casual employees employed on a regular or systematic basis). Therefore, previously if your business was not considered a small business due to the number of employees, now your business if it satisfies the test, will be considered a small business.

Key Change No.4

From 5 April 2021, ASIC expects all insurers to ensure that consumer and small business standard form contracts **have been reviewed** for *fairness* and that they obtain their own legal advice in relation to potential unfair contract terms where needed. ASIC has said it will continue to monitor insurance contracts for unfair terms and will consider the range of their regulatory powers where they are concerned about non-compliance and consumer harm.

Key Change No.5

A 'standard form contract' is a contract that has been prepared by one party to the contract (the business offering the product or service) *without* negotiation between the parties. In other words, it is offered on a 'take it or leave it' basis. However, the UCT law will improve clarity on when the protections apply and *consider* whether a small business had an **effective opportunity to negotiate the contract**, including the opportunity for small business to negotiate in the future.

For example, Body Repairer A is a network repairer for Insurance Company B and their contract is coming up for renewal. No longer should the contract be on a "take it or leave it" basis, as Repairer A must be provided with sufficient opportunity to negotiate on the terms of the contract (the agreement) with Insurer B. This was previously not allowed or limited with standard insurance network agreements provided to repairers. The insurer with limited or no room for negotiation on the terms, would present a contract to a repairer expecting a repairer to accept it as it is. This should not be occurring and may be considered *unfair*, if post signing of the contract it would be found that a term is unfair in the contract and no reasonable steps for negotiation were offered to the repairer. In short, any business-to-business agreement can now be negotiated, even if in a 'standard form contract' as both parties should be afforded the opportunity to negotiate on the terms as required.

Courts will have more flexible remedies when they declare contract terms unfair. The broader application of the laws and the threat of a civil penalty (yet to be confirmed) should encourage businesses, like large insurers to review their contracts in a timely manner and allow sufficient negotiations between both parties.

In addition, any business that is a small business commonly enters standard form contracts for financial products and services such as contracts for business loans, credit cards, insurance cover or broker agreements. The UCT laws extend not only to a repairer's contract with an insurer, but other financial providers as well.

If a small business alleges that a contract is a standard form contract, the contract is presumed to be a standard form contract unless proven otherwise.

Key Change No.6

A Presumption of *unfairness*

A term will be presumed to be unfair if the same or a substantially similar term was found to be unfair in similar circumstances in a separate case. This highlights the fact that only one small business needs to challenge a term in a standard form contract (for example, provided by an insurer to a 'network repairer'), and if successful (as precedent) it would be highly likely to be also found unfair for many other small business owners with the same or similar contract. If as a small business, you know another small business that has the same 'standard form contract' the upcoming **collective bargaining class exemptions** may be useful for you. The class **exemption** removes the risk that **collective bargaining** by eligible businesses will breach the competition laws in Australia. The Australian Competition and Consumer Commission (ACCC) is yet to set a commencement date for the class exemption, but it is expected to come to fruition late 2021.

More information on collective bargaining will be provided by VACC to its members once available.

Key Change No.7

Greater access to remedies

Currently, courts are able to make orders against a contractual party where they have been unfairly *advantaged* by an unfair term to redress loss or damage incurred by a class of persons (including "non-party consumers", namely consumers that may not be part of the legal action but were subject to the term by way of standard form contract). The government has proposed expanding the scope of persons who can access remedies for a breach of the unfair term regime by clarifying that remedies that are available to "non-party consumers" are also available to "non-party small businesses".

Key Change No. 8

Intermediated sale – the Broker.

Although there was some guidance in the draft consultation materials, the government has not provided more clarity in relation to when an insurance contract ceases to be a standard form contract. An insurance contract can still be a standard form contract if a **broker** acts on behalf of the customer. However, brokers frequently seek specific endorsements on behalf of their clients. In some circumstances, these negotiated contracts may no longer be a standard form contract.

As a result of the new laws, small businesses (like a body repairer) who has a customer through a broker should be aware, as should the customer, of who the broker acts for during any negotiation of the insurance policy terms, if the terms become an issue in the claims process.

Small business repairers should be aware that because the broker has familiarity with the system and the insurance company, they **can and in many cases should** expertly manage any claim they take on and any disputes that may arise. Brokers are skilled in getting **claims** processed painlessly and paid quickly and should not hide in an issue that arises when a term may be considered unfair in a contract between an insured and an insurer. Small business repairers should utilise any broker that should be working in the insured's best interest in a claim matter and or if an unfair term in the insurance contract arises. Please ask your customers if their policy was sold via a broker. A broker should be representing the customer, not the insurer once a claim arises and can prove a vital ally in a claims dispute or if a unfair term is identified as part of the claims process in the customers contract of insurance.

Next week, Unfair Contract Terms Part 3: What a small business can do if they think a contract term is unfair and potential penalties for using an unfair term.

Important Notice

Please note that the information is a summary giving you basic information about a particular topic. It does not cover the whole of the relevant law regarding that topic, and it is not a substitute for professional advice.

You should also note that because this information sheet avoids legal language wherever possible, it might include some generalisations about the application of the law. Some provisions of the law referred to have exceptions or important qualifications. In most cases, your particular circumstances must be considered when determining how the law applies to you.

If you need further information, please contact me on 03 9829 1142.

Kind regards

Kathy Zdravevski LLM(JD)
Industry Policy Advisor – Industry Divisions
BRD, TOD

VACC

Level 7 | 464 St Kilda Road | Melbourne Vic 3004
P: 03 9829 1142 | M: 0418 329 527 | W: vacc.com.au