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21 December 2018

Ruth Moore
Manager
Unfair Contract Terms Review
Consumer and Corporations Policy Division
The Treasury
Langton Crescent
PARKES ACT 2600

By email: consumerlaw@treasury.gov.au

Dear Ms Moore

Review of Unfair Contract Term Protections for Small Business

The ACCC welcomes the opportunity to make a submission to the Review of Unfair Contract Term Protections for Small Business. Our submission is attached to this letter.

As set out in our submission, the ACCC's principal recommendation is that the inclusion of an unfair contract term (UCT) in a standard form contract should be a contravention of the CCA and subject to civil pecuniary penalties and other remedial orders commonly available to the court for contraventions of the ACL.

The ACCC's experience with enforcing and promoting compliance with the current UCT provisions indicates that businesses currently have little incentive to offer standard form contracts that comply with the law and, consequently, compliance and enforcement action by regulators in this area has minimal deterrent effect.

In addition to our principal recommendation, the ACCC makes a number of other recommendations to help clarify and improve the UCT regime. While the ACCC considers that these additional recommendations will assist in clarifying and improving the UCT provisions, they will not solve the key issue of improving compliance to ensure that small businesses receive the law's protections.

If you wish to discuss any aspect of the attached submission, please contact Gabrielle Ford, General Manager Advocacy, International and Agriculture Branch, on (03) 9290 1942 or gabrielle.ford@accc.gov.au.

Yours sincerely

Rod Sims
Chair

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Review of Unfair Contract Term Protections for Small Business

ACCC Submission

21 December 2018

Summary

The ACCC is responsible for enforcing and promoting compliance with the *Competition and Consumer Act 2010* (Cth) (CCA), including the Australia Consumer Law (ACL) that contains the unfair contract terms (UCT) provisions. On 12 November 2016, the UCT provisions in the ACL were extended to cover some business-to-business contracts.

The business-to-business unfair contract terms law is a valuable law that is intended to protect small businesses against unfair terms in standard form contracts. Parliament extended the provisions out of recognition that small businesses, just like consumers, frequently lack the bargaining power, time and expertise to negotiate or assess all standard form contracts for potential UCTs. UCTs often allocate contract risks to the party that is least able to manage them. Small businesses are less likely to be able to adopt robust risk management strategies to absorb unreasonable risk allocations under a contract. The extension of the UCT provisions to small business standard form contracts was intended to deter the inclusion of UCTs in these contracts and therefore provide for more efficient contracting and risk allocation.[1]

However, the protection offered to small businesses by the UCT provisions is undermined by fundamental limitations with the current regime, namely:

- There is little incentive for businesses offering standard form contracts to comply with the law, since the inclusion of UCTs in standard form contracts is not a contravention of the ACL and the court cannot impose a penalty on a business that includes UCTs in its standard form contracts.
- As a result, compliance and enforcement action by regulators has minimal deterrence.

These limitations mean that in spite of the UCT provisions and considerable ACCC compliance and enforcement action, UCTs continue to exist in a significant number of business-to-business standard form contracts.

From the ACCC's compliance and enforcement experience to date, unfair contract terms are causing real detriment to small businesses, particularly in concentrated industries where small business suppliers or acquirers need to maintain an ongoing supply relationship with a large business to remain viable.

As this submission details, the ACCC expends a large amount of resources on investigating and trying to resolve business-to-business UCT issues. Given the way the current UCTs regime operates, the ACCC is required to attempt to resolve UCT matters before it can resort to litigation, which can often be a time consuming and resource intensive process. As the ACCC is unable to institute proceedings in relation to the prior use of the potential UCT once it has been corrected, this creates an incentive for the business imposing the UCT to change the term at the last minute to avoid court proceedings, and after the ACCC has expended considerable resources.

Any positive outcomes from this process are mostly limited to that particular business subject to ACCC investigation, because the current regime provides very weak incentives for broad business compliance with the laws. As such, the current regime poses significant problems from the perspective of both business compliance and ACCC resourcing.

From 2016 to date, the ACCC has prioritised action to ensure that small businesses receive the protections of the unfair contract terms law,[2] and has been the main ACL regulator enforcing compliance with the unfair contract terms law. While the ACCC is expending these resources in

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[1] https://parlinfo.aph.gov.au/parlInfo/download/legislation/ems/r5497_ems_b35077f3-dbb6-4c5a-81b0-7b885634fd81/upload_pdf/503040.pdf;fileType%3Dapplication%2Fpdf

[2] Ensuring small business receive the protections of the UCT law has been a priority area for the ACCC in 2016, 2017 and 2018. See https://www.accc.gov.au/system/files/2016%20ACCC%20Compliance%20and%20Enforcement%20Policy_0.pdf; https://www.accc.gov.au/system/files/ACCC%20Compliance%20and%20Enforcement%20Policy%202017.pdf; and https://www.accc.gov.au/system/files/D18-20423%20Enf%20-%20Admin%20Other%20-%20CLEAN%20VERSION%20final%20draft%20Combined%20Complia....pdf

investigating business-to-business UCT issues, these are resources that the ACCC is unable to use elsewhere in enforcing and promoting compliance with the CCA.

The ACCC's compliance and enforcement experience with the UCTs regime forms the basis of this submission's principal recommendation to the Review.

Principal Recommendation

The inclusion of a UCT in a standard form contract should be **a contravention of the ACL** and subject to **civil pecuniary penalties** and other remedial orders commonly available to the court for contraventions of the ACL.

Additional recommendations

In addition to the principal recommendation, this submission makes a number of additional recommendations to help clarify and improve the UCT regime. Whilst the ACCC considers that these additional recommendations will assist in clarifying and improving the UCT regime, they will not solve the key issue of improving compliance with the UCT regime to ensure that small businesses receive its protections. The ACCC's Principal Recommendation is the necessary and most effective way to drive compliance with the laws.

Additional Recommendation 1

The ACL should be amended to make **more flexible remedies** available for the court to order when it determines that a term in a standard form contract is unfair. For example, section 239 of the ACL could be amended to extend its application to business-to-business standard form contracts.

Additional Recommendation 2

The **threshold** requirements for the UCT provisions should be reconsidered.

A clearer and more effective threshold for the application of the UCT regime would be for it to apply to standard form contracts entered into by **businesses with less than $10 million annual turnover**.

Additional Recommendation 3

The UCT provisions should be amended to **better clarify the concept of 'an effective opportunity to negotiate'**.

Scope of the existing UCT regime

For small businesses, the UCT regime in the ACL applies to standard form contracts entered into or renewed on or after 12 November 2016, where:

- it is for the supply of goods or services, or the sale or grant of an interest in land
- at least one of the parties is a small business (employs less than 20 people, including casual employees employed on a regular and systematic basis); 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.

If a contract is varied on or after 12 November 2016, the law applies to the varied terms.

The ACL provides guidance on what constitutes a 'standard form contract'. Broadly, it is one that has been prepared by one party to the contract and where the other party has little or no opportunity to negotiate the terms – that is, it is offered on a 'take it or leave it' basis.

The UCT regime also applies to business-to-consumer standard form contracts.

While this submission will focus on the ACCC's experience and recommendations in relation to business-to-business UCTs, the ACCC's Principal Recommendation applies with equal force to business-to-consumer standard form contracts.

Compliance and enforcement activity

Education and liaison activities

In the lead-up to the business-to-business UCT provisions taking effect, the ACCC examined standard form contracts in the advertising, telecommunications, retail leasing, independent contracting, franchising, waste management, and agriculture industries, aiming to identify terms that may be considered unfair contract terms post 12 November 2016.

On 10 November 2016, the ACCC published a report into potential UCTs that it identified as part of its review of 46 contracts across seven industries.[3] The ACCC published the Unfair Terms in Small Business Contracts report to encourage businesses, particularly in the industries specifically covered by the report, to review their contracts. The report also noted the ACCC compliance work done up to that date, and that a number of businesses had amended their contracts after being contacted by the ACCC.

The ACCC's review and report was designed to assist industry with identifying terms that the ACCC would consider potentially unfair. It included specific examples, such as unilateral variation clauses, indemnity clauses, automatic renewal clauses and burdensome termination clauses. It also included commentary on why the ACCC considered terms of this nature may be unfair.

The ACCC sent its report to businesses in the specific industries cited in the report. It also distributed the report through its existing business networks to put as many parties as possible on notice of the changes to the law.

Contacts received

Since 12 November 2016, the ACCC has received approximately 950 contacts about potential UCTs in business-to-business standard form contracts.

The high number of contacts shows that there is significant concern about UCTs in standard form business-to-business contracts. The ACCC believes that the number of potential business-to-business UCTs in current use is likely to be higher than is reflected in the number of contacts, as many small businesses may still be unaware of the UCT provisions.

ACCC's approach to compliance and enforcement

The ACCC's role is to focus on those circumstances that will, or have the potential to, harm the competitive process or result in widespread consumer detriment. Therefore, the ACCC exercises its discretion to direct resources to matters that provide the greatest overall benefit for competition and consumers, and it is selective in the matters it investigates and the sectors in

[3] https://www.accc.gov.au/publications/unfair-terms-in-small-business-contracts

which it engages in education and market analysis. The ACCC rarely becomes involved in individual consumer or small business disputes. Prioritisation of the matters pursued is conducted in accordance with the ACCC's Compliance and Enforcement Policy.[4] The ACCC's 2018 priorities include ensuring small business receives the protections of the UCT provisions.

The ACCC has a range of compliance and enforcement tools available to encourage compliance with the laws we enforce. In deciding which compliance or enforcement tool (or the combination of tools) to use, the ACCC's first priority is to achieve the best possible outcome for the community and to manage risk proportionately. The tools available to the ACCC to encourage compliance are, however, limited by the remedies available in the laws we enforce.

ACCC enforcement action relating to the business-to-business UCT provisions

As noted in the Review's discussion paper, since 12 November 2016 the ACCC has successfully taken two businesses to court regarding UCTs in their standard form contracts with small businesses, and has ongoing litigation in relation to one other.

The ACCC has also entered into court enforceable and administrative resolutions with a number of companies, pursuant to which the companies agreed to amend terms the ACCC considered likely to be UCTs.

Litigation

JJ Richards & Sons Pty Ltd

In September 2017, the ACCC commenced proceedings against JJ Richards & Sons Pty Ltd in relation to alleged UCTs in its waste management contracts with small businesses. The ACCC alleged that eight terms, including terms allowing unilateral price increases, automatic rollovers, and unlimited indemnity in favour of JJ Richards, were UCTs and therefore void. On 19 October 2017, the Federal Court declared, by consent, that all eight terms were unfair and therefore void.

Servcorp Parramatta Pty Ltd and Servcorp Melbourne 18 Pty Ltd

On 15 September 2017, the ACCC commenced proceedings against these Servcorp subsidiaries for alleged UCTs in their contracts with small businesses relating to the provision of office space and virtual office services such as office suites, secretarial services, IT, communications and personal assistants to its clients.

On 13 July 2018, the Federal Court declared, by consent, that 12 terms in Servcorp's standard form contracts were unfair and therefore void. These terms included unilateral price increases, automatic renewals, unreasonable limitations on Servcorp's liability or imposing unreasonable liability on the customer, unreasonable penalty and unreasonable termination clauses.

Mitolo Group Pty Ltd and a related entity

On 26 June 2018, the ACCC commenced proceedings against Mitolo Group Pty Ltd and a related entity alleging that several terms in Mitolo's standard form contracts with potato farmers are unfair contract terms.

The alleged UCTs include terms that allow Mitolo to unilaterally determine or vary the price Mitolo pays farmers for potatoes, unilaterally vary other contractual terms, declare potatoes as 'wastage' without a mechanism for review, and prevent farmers from selling surplus potatoes to alternative purchasers. The ACCC also alleges that a term preventing farmers from selling their

[4] https://www.accc.gov.au/about-us/australian-competition-consumer-commission/compliance-enforcement-policy-priorities

own property unless the prospective purchaser enters into an exclusive potato farming agreement with Mitolo is unfair.

The Mitolo litigation is ongoing.

Court enforceable undertakings and administrative resolutions

In May 2017, **Sensis Pty Ltd** agreed to amend particular terms in its product contract terms that the ACCC was concerned were likely to constitute UCTs once the legislation commenced.[5]

On 26 March 2018, the ACCC accepted a court enforceable undertaking from **Cardtronics Australasia Pty Ltd** regarding UCTs in contracts governing non-bank ATMs deployed on the premises of small businesses. The relevant contract terms the ACCC considered to be unfair included automatic contract renewal, unilateral fee increases and first right of refusal when renegotiating contracts.

On 14 March 2018, the ACCC announced that, following an ACCC investigation, grain marketing organisation **AWB Harvest Finance Pools Pty Ltd** (AWB) had made changes to its standard form grain pool contracts to address the ACCC's concerns that terms allowing AWB to unilaterally increase fees to growers and introduce new fees to growers after the contracts had been signed, and terms allowing AWB to reject grain at its absolute discretion, were unfair.

On 2 July 2018, the ACCC announced that, following an ACCC investigation, **Warrnambool Cheese and Butter Factory Company Holdings Limited** (WCB) had altered terms in its milk supply agreements and milk supply handbook. The ACCC considered that the following terms in WCB's contracts with farmers were UCTs:

- terms that allowed WCB to unilaterally vary the milk price and other milk supply terms, with farmers unable to terminate the milk supply agreement early without incurring a financial penalty, and
- terms that placed restrictions on farmers selling their farm and required farmers to indemnify WCB for loss which could be avoided or mitigated by WCB.

On 3 December 2018, the ACCC announced that, following an ACCC investigation, **Visy Paper Pty Ltd** (trading as Visy Recycling), **Cleanaway Pty Ltd** and **Suez Recycling & Recovery Pty Ltd** have reviewed and amended potentially unfair contract terms in their standard form contracts. These included terms that allowed these waste management companies to unilaterally increase their prices in specified circumstances and impose unreasonable penalties on customers who wanted to exit their contracts before the end of the contract term. The ACCC continues to investigate the use of potentially unfair contract terms in the waste management industry.

On 3 December 2018, the ACCC also announced that, following an ACCC investigation, dairy processors **Brownes Food Operations**, **Lion Dairy & Drinks**, **Norco Co-operative Limited**, **Parmalat Australia** and **Fonterra Australia** have agreed to amend specific terms in their milk supply agreements to address the ACCC's concerns that these terms were unfair to their dairy farmer suppliers. The terms that the ACCC raised concerns about included terms that allowed the processors to unilaterally vary supply terms (such as price or quality requirements), lengthy notice periods for farmers to terminate their contracts, one-sided termination rights, broad indemnities, and terms that restrict a farmer's ability to lease a farm or sell their cattle.

[5] At the same time, the ACCC also accepted a court enforceable undertaking from Sensis Pty Ltd in relation to concerns that it had engaged in misleading or deceptive conduct in relation to its automatic renewal and cancellation processes.

Principal Recommendation

The inclusion of a UCT in a standard form contract should be **a contravention of the ACL** and subject to **civil pecuniary penalties** and other remedial orders commonly available to the court for contraventions of the ACL.

The ultimate goal of the UCT laws should be to deter the use of UCTs so that businesses using standard form contracts with consumers and small businesses will, without prompting from the ACCC or other regulators, take steps to ensure that their standard form contracts are fair. As they currently stand, the UCT laws do not achieve this basic objective.

This is because a business can include a UCT in its standard form contract and incur little to no risk of adverse consequences. Including UCTs in standard form contracts is not a contravention of the ACL and the worst outcome for a business that has a UCT in its standard form contract is that a court declares that clause unfair and therefore void.

From the ACCC's experience in its compliance and enforcement work in this area, the ACCC strongly recommends that the UCT provisions in the ACL should be amended to:

- make inclusion of a UCT in standard form contracts entered into with a small business or with a consumer a contravention of the ACL; and
- allow for the court to impose civil pecuniary penalties, and other remedial orders which are commonly available to the court for contraventions of the ACL (e.g. injunctions, adverse publicity orders, compensation orders, and community service orders), where a breach of the UCT provisions is established.

The absence of penalties creates an inadequate framework for compliance

The current UCT provisions place a significant burden on the ACCC, or a party subject to a UCT, to enforce the provisions, while providing little to no incentive for businesses to proactively assess their standard form contracts for fairness. This is poor regulatory design, as it necessitates enforcement to achieve compliance with the law.

This design has significant flow-on effects for the ACCC, and for consumers and small businesses who may wish to challenge terms in a standard form contract as unfair.

Businesses should take responsibility for their compliance obligations, rather than the ACCC bearing this responsibility

As large businesses currently face limited consequences for including UCTs in their standard form contracts, they have weak incentives to make their contracts compliant before coming to a regulator's attention. The ACCC's repeated experience has been that under this framework UCTs will persist in an industry despite consultation with businesses and enforcement action.

The result is that the ACCC is required to become a "compliance officer" for businesses. Instead of businesses assessing their own contracts for fairness in order to avoid potential regulatory attention, the business can continue to use potentially unfair contracts until a regulator expresses concern. In practice, resource limitations mean any compliance that the ACCC can achieve by its enforcement actions is limited to the particular business in question, and therefore many UCTs in use will not be subject to scrutiny.

This is exacerbated by legislative issues that minimise the likelihood of court action being commenced against businesses that use potential UCTs. As there is no civil pecuniary penalty available in relation to the use of UCTs, the *Civil Dispute Resolution Act 2011* (Cth) requires the ACCC to take genuine steps to resolve the dispute prior to litigation. This requirement means that, even in the most egregious cases, the ACCC must raise concerns with a business about

potential UCTs and seek its response. This leads to protracted negotiations where the business may:

- make piecemeal amendments that do not fully address the ACCC's concerns, and/or
- claim that a term is necessary to protect its legitimate interests and therefore not a UCT, but not provide adequate information to demonstrate this.

The ACCC will continue to engage with the business to satisfy the 'genuine steps' requirement, and this often leads to administrative outcomes rather than litigation.

If the ACCC does face a business that is particularly unwilling to engage with the ACCC's concerns, the business can wait to see if the ACCC will litigate before taking steps to amend its contracts. Some businesses offer to amend contract terms only once the ACCC advises that it is considering or intending to commence court proceedings against them. Given that the inclusion of a UCT in standard form contracts is not a contravention of the ACL, once the potential UCTs are amended, the ACCC no longer has a legal cause of action against the business, even though it had been using potential UCTs in its standard form contracts right up until that point. By this time, the ACCC has incurred significant legal and other resourcing costs that cannot be recovered.

This leads to two key issues:

1) Administrative outcomes do not result in effective general or specific deterrence. This is discussed further below.

2) While the ACCC is expending significant resources to obtain a non-court based outcome that has a less significant effect on compliance and deterrence, these are resources that the ACCC is unable to use elsewhere in enforcing and promoting compliance with the CCA.

General deterrence in an industry is difficult to achieve under the current UCT regime

The lack of incentives for business compliance makes ACCC compliance and enforcement work within and across industries less effective. Before and after the business-to-business UCT provisions came into effect, the ACCC made a concerted effort to educate businesses and industry groups to put them on notice of the introduction of the law, the ACCC's expectations for compliance, and even to highlight specific UCT issues identified in problematic industries. Despite this outreach and compliance work, the ACCC has had to invest significant time and resources into enforcement action, including in industries and against traders who were specifically put on notice of the changes.

Even after the ACCC has achieved a litigated outcome or a public administrative resolution related to UCTs, broader industry change can be difficult to achieve. The ACCC's actions in the waste management industry provide an illustrative example.

The first court action taken by the ACCC in relation to business-to-business UCTs was against the waste management provider JJ Richards and Sons Pty Ltd in September 2017. The terms in JJ Richards' standard form contracts declared to be UCTs included terms allowing unilateral price increases, automatic rollovers, and unlimited indemnity in favour of JJ Richards.

The ACCC had specifically noted its concerns with terms like these in the waste management industry in its 10 November 2016 Unfair Terms in Small Business Contracts report.

After the JJ Richards matter concluded, the ACCC wrote to waste management providers to put them on notice of the decision and encourage them to revise their contracts. Nonetheless, the ACCC has had to continue its compliance work in the waste management industry for over a year after the JJ Richards decision.

On 3 December 2018, the ACCC issued a media release noting that Visy Paper Pty Ltd (trading as Visy Recycling), Cleanaway Pty Ltd and Suez Recycling & Recovery Pty Ltd have reviewed and amended potentially unfair contract terms in their standard form contracts following an ACCC investigation. The alleged UCTs once again included unilateral price variations, as well as terms allowing them to impose unreasonable penalties on customers who wanted to exit their contracts before the end of the contract term. While these parties ultimately cooperated with the ACCC, it was only after the ACCC raised concerns, and had considerable engagement with them, that they amended their contracts.

The ACCC's experience in the waste management industry demonstrates non-compliance is not due to a lack of clarity about what constitutes a UCT. The ACCC has engaged extensively with the waste management industry and obtained declarations that certain terms in a major waste management provider's contract were unfair. These court orders were obtained despite the issues noted above, all of which make an administrative resolution the more likely outcome in a UCT investigation. Despite the ACCC's educative efforts and the declarations from the court in the JJ Richards case, UCTs persisted in this industry.

If the inclusion of UCTs in a standard form contract was a contravention of the ACL and subject to a potential pecuniary penalty, this would provide stronger incentives for businesses to:

- monitor developments in their industry and UCT laws generally
- review standard form contracts, and
- make changes to standard form contracts where necessary,

in order to avoid potential regulatory action.

Repeated use of UCTs

Under the current regime, if the court finds that a business has included UCTs in its standard form contract with one small business customer, that business could still include similar or other UCTs in standard form contracts with other small business customers, or in future standard form contracts, and face few consequences. It is not clear the extent to which an injunction from the court can cover the use of similar UCTs in the business's standard form contracts more generally. It is likely that an injunction in these circumstances is limited to the precise clause(s) the subject of the litigation. This means a business could make slight changes to the relevant term that do not change the substance or effect of the term, and this may not be covered by the injunction.

This is a particularly high risk for businesses with low public profiles that would suffer little reputational risk from continuing to use UCTs. This would force the ACCC to incur repeated compliance and enforcement costs to deal with repeat offenders.

Penalties are appropriate for UCTs

It should be the responsibility of the business offering a standard form contract to ensure it does not contain UCTs. This is an appropriate allocation of responsibility as these businesses are in the best position to determine what risk allocation is efficient and fair under the contract, and align the obligations under the contract with their own business practices. These businesses are also in the best position to know which contract terms they are willing to negotiate on, whether a small business customer or supplier could actually carry the risks incurred by a potential UCT, and what other risk mitigation strategies could be adopted.

The lack of penalties for including UCTs in a standard form contract has an impact across the economy, and undermines the regime's effectiveness for small businesses and consumers alike. UCTs continue to exist in small business and consumer standard form contracts across the Australian economy, and the ACCC is not able to take effective compliance and enforcement action to motivate businesses to eliminate such terms. For example, as noted in preliminary

recommendation 5.5 of the ACCC's Digital Platforms Inquiry, the current standard form contracts used by digital platforms contain a number of possible UCTs related to their use of a user's data. The potential for pecuniary penalties could force digital platforms to revisit their standard form contracts and narrow the rights they have to a user's data.

Amending the ACL to allow for the court to impose civil pecuniary penalties, and other remedial orders which are commonly available to the court for contraventions of the ACL, would not produce unreasonable outcomes:

- The ACCC (or a consumer or small businesses who may wish to challenge terms in a standard form contract as unfair) would still be required to establish that a term is a UCT, using the current meaning of 'unfair' under section 24 of the ACL – i.e. that it causes a significant imbalance in the parties' rights and obligations; that it is not reasonably necessary to protect the legitimate interests of the party advantaged by the term, and that it causes financial or other detriment to the other party to the contract if it were relied on.
- As with all other pecuniary penalties available under the ACL, the court would still need to:
    - be satisfied that imposing a pecuniary penalty is appropriate in the circumstances of any individual case, and
    - determine the appropriate penalty amount to be imposed in the circumstances of any individual case, following legal principles on penalty from well-established case law.

Standard form contracts are generally used by large businesses in dealings with small businesses and consumers that have little to no countervailing bargaining power. The UCT regime recognises that this can lead to unfair outcomes for those small businesses and consumers. If the objective of the UCT regime is to make standard form contracts fair, the only effective way to achieve that is to make the inclusion of UCTs in a standard form contract a contravention of the ACL and subject to potential civil pecuniary penalties.

Additional Recommendations

Additional Recommendation 1

The ACL should be amended to make **more flexible remedies** available for the court to order when it determines that a term in a standard form contract is unfair. For example, section 239 of the ACL could be amended to extend its application to business-to-business standard form contracts.

Currently, if a court declares a term of a standard form contract unfair, that term is then considered void. Section 250 of the ACL allows a regulator to seek a declaration from a court that a term is unfair, which by operation of section 23 of the ACL means that the term is void. Following this outcome, where the standard form contract is capable of operating without the unfair term, it will continue to bind the parties. However in some instances, removal of the relevant term may result in uncertainty for the parties.

The court should be able to order more flexible remedies than just declarations. This could be achieved by extending the application of section 239 of the ACL to business-to-business UCTs. Section 239 of the ACL allows the court to make orders for consumer redress where a declaration is made under section 250 in relation to a business-to-*consumer* standard form contracts. Such orders can include an order varying a contract or arrangement.[6]

If more flexible remedies were available to the court, this would overcome the sometimes uncertain or unintended consequences that may result from a declaration that a term in a business-to-business standard form contract is unfair and therefore void under section 23 of the

[6] Section 243 of the Australian Consumer Law.

ACL. For example, in some matters the ACCC has investigated, the ACCC considered that the termination clauses used in standard form contracts were likely to be unfair because they imposed disproportionate or unreasonable costs for termination, or imposed unreasonable notice periods, on small business customers / suppliers. In response to the ACCC's queries, some businesses have raised the legitimate concern that if a termination clause is declared unfair, and therefore void, the contract would be left with no termination clause at all, and this would be an even more unfair position.

While in such circumstances, a court may determine that the relevant contract is not 'capable of operating' without the void term, there has been little judicial consideration of this in the area of business-to-business unfair contract terms. This creates uncertainty for all parties to the contract.

Alternatively, if the entire contract is found not to be capable of operating without the void term, this could also have a detrimental impact on all parties to the contract, but particularly to the parties that are small businesses or consumers. There can be meaningful transaction and administrative costs involved in signing up to a new contract and the business imposing the standard form contract may refuse to supply or acquire critical goods or services from the small business until it signs a new contract.

In consideration of potential uncertain or harmful outcomes, the ACCC has, at times, declined to take action against potential UCTs, as the outcome may be worse for the small businesses than the effect of the term itself.

If the unfair term is part of a business-to-consumer standard form contract, in addition to seeking a declaration that a term is unfair under section 250, a regulator can also apply for non-party redress orders under section 239 of the ACL. Amending section 239 of the ACL to extend it to business-to-business standard form contracts would allow the court to vary the business-to-business standard form contract in question, as it sees fit.

This amendment could be an effective way to allow for more flexible and mutually beneficial outcomes than voiding the term or contract as a whole. For example, the court could order that a standard form contract is varied to include a new, fair termination clause.

Additional Recommendation 2

The **threshold** requirements for the UCT provisions should be reconsidered.

A clearer and more effective threshold for the application of the UCT regime would be for it to apply to standard form contracts entered into by **businesses with less than $10 million annual turnover**.

As noted above, the current UCT provisions apply to business-to-business standard form contracts where:

- at least one of the parties is a small business (employs less than 20 people, including casual employees employed on a regular and systematic basis); 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.

According to the Explanatory Memorandum, these two thresholds were intended to serve different policy purposes. The employee count threshold was intended to identify those businesses that are small and likely to require the protections of the UCT regime. The upfront price payable threshold was intended to limit the UCT regime so that it would not apply to high-

value contracts entered into by small businesses, as it is reasonable to expect small businesses would undertake due diligence for such contracts.[7]

The ACCC's compliance and enforcement experience suggests that these thresholds may not be fit for purpose, and may be excluding small business standard form contracts to which the UCT regime should apply. Issues the ACCC has seen with these thresholds are discussed further below.

Additionally, the ACCC questions the utility of having thresholds for 'small business' and 'upfront price payable' at all. The UCT provisions only apply to standard form contracts. Where a business can impose a contract on a 'take it or leave it' basis, it demonstrates that the other business lacks countervailing bargaining power or any ability to effectively negotiate, such that the UCT protections should apply to that contract. Further, if a small business contract is truly a standard form contract with no effective opportunity for that small business to negotiate the terms, then this greatly limits the impact of any due diligence that the small business can undertake (such as seeking legal advice), no matter the value of the contract. This is particularly the case in concentrated industries where small business suppliers or acquirers lack viable alternatives.

Nevertheless, the ACCC appreciates that a clear threshold may assist businesses in understanding whether their contracts are covered by the business-to-business UCT regime.

The ACCC considers that a clearer and more effective threshold in order for the UCT regime to cover the small business contracts that should receive its protections would be for it to apply to standard form contracts entered into where one of the parties to the contract is a business with less than $10 million annual turnover. This is the Australian Taxation Office's definition of a small business for tax purposes.

This threshold would allow for easier identification of the relevant party to a standard form contract as a small business, as a business customer is likely to know if they are a small business for tax purposes. It would also capture more businesses that operate in labour-intensive, low revenue industries. Finally, a turnover test is likely to better reflect the ability of those businesses to absorb and account for risk.

While the business offering a standard form contract would not be able to independently determine whether its small business customers / suppliers are under a $10 million annual turnover threshold, this could easily be determined by asking whether the customer / supplier is a small business for tax purposes.

Issues with the employee numbers threshold

The current metric of employee numbers is not fit for purpose as an eligibility threshold for the business-to-business UCT regime. The 'less than 20 employees' approach was based on the Australian Bureau of Statistics' approach to defining small businesses, and was not specifically designed for the UCT regime's objectives.[8]

Any business contracting with a smaller business is unable to conveniently determine that business's employee headcount. Further, a small business owner may not know whether their casual employees meet the legal test of 'employed on a regular and systematic basis'. This test is based on relatively complex employment law, and is still subject to uncertainty.

In the ACCC's compliance and enforcement experience with the UCT regime, there are businesses in some industries, for example hospitality and road transport, where it is common

[7] https://parlinfo.aph.gov.au/parlInfo/download/legislation/ems/r5497_ems_b35077f3-dbb6-4c5a-81b0-7b885634fd81/upload_pdf/503040.pdf;fileType%3Dapplication%2Fpdf

[8] See paragraph 3.126 of the Explanatory Memorandum at https://parlinfo.aph.gov.au/parlInfo/download/legislation/ems/r5497_ems_b35077f3-dbb6-4c5a-81b0-7b885634fd81/upload_pdf/503040.pdf;fileType%3Dapplication%2Fpdf

for businesses to engage a large number of casual employees on a regular and systematic basis. However many of the businesses in these industries have all the hallmarks of the very businesses the UCTs regime was designed to cover, i.e. they:

- hold little to no countervailing bargaining power when faced with a standard form contract,
- lack the time and expertise to negotiate or assess all standard form contracts for potential UCTs,
- are unlikely to be able to adopt robust risk management strategies to absorb unreasonable risk allocations under a contract.

Issues with the upfront price payable threshold

As noted above, the upfront price threshold was intended to maintain the onus on small businesses to undertake due diligence for high-value transactions.[9]

However in many circumstances, a business will face no meaningful choice about whether to sign a standard form contract, making due diligence (such as seeking legal advice) only of limited benefited. Where a small business undertakes due diligence and is in a position to negotiate amendments to a contract, that contract will no longer be a standard form contract and will not be captured by the UCT provisions. This means the only effect of the upfront value threshold is that parties who are not in a position to negotiate because of a lack of bargaining power and face no meaningful choice are forced to sign high value contracts that contain UCTs. This has a particularly significant impact on high revenue, low margin businesses, such as farming.

Aside from this issue, as currently drafted, the UCT provisions are unclear about how the 'upfront price payable' under the contract should be determined where the price under the contract is indicative, or estimated and subject to change depending on market conditions, or variable subject to supply volumes and market conditions. These forms of pricing are common across a number of industries, particularly in agriculture, and the ACCC has been faced with circumstances where the application of the UCT provisions is unclear due to such pricing structures.

Given the lack of clarity in these circumstances, this could create an opportunity for businesses to circumvent the UCT provisions through the way in which they structure the price payable under their standard form contracts.

In June 2018, the ACCC took action against Mitolo in relation to potential UCTs in its contracts with potato farmers. The Mitolo contracts included, among other alleged UCTs, the power for Mitolo to unilaterally determine and vary the price at which they will purchase potatoes from farmers. At the time a farmer signs a contract with Mitolo, there would be no immediately calculable upfront value, as the price for the potatoes is not determined and the future value of the produce is unknown. The ACCC has taken the view that if there is no immediately calculable upfront value, then the contract falls within the UCT regime's upfront price payable threshold.

While the ACCC considers that the Mitolo contracts fall within the UCT regime, the courts have yet to provide authority on the issue.

The ACCC notes that the current upfront price payable threshold excludes a large number of contracts in industries with high turnover and low margins where it may be appropriate to apply the UCT provisions to at least some of the businesses in such industries. This is particularly relevant to agricultural contracts, when farmers sign up to high value contracts with processors or other buyers. These contracts have all the hallmarks of a small business to large business contract that the UCT regime was intended to cover, as many farmers:

[9] Ibid, paragraph 2.7 of the Explanatory Memorandum.

- lack the time and expertise to negotiate or assess the contract for UCTs,
- lack any real countervailing bargaining power, and
- cannot easily absorb unreasonable contract risks.

Additional Recommendation 3

The UCT provisions should be amended to provide **better clarity on the concept of 'an effective opportunity to negotiate'**.

A UCT will only be void when it is included in a standard form contract. Whether a contract is standard form is determined by reference to the factors in section 27 of the ACL. These factors include whether a party was given an effective opportunity to negotiate the terms of the contract.

The ACCC has seen a number of instances in business-to-business contracts where a large business provides its contract on a 'take it or leave it basis', with no opportunity to negotiate for the vast majority of its small business customers. However a small subset of small business customers are able to negotiate limited changes. For example, a small business customer may negotiate to remove an automatic rollover clause because they only need the services for a short time. It is unclear whether these circumstantial negotiations allow a business to argue their contract is no longer a 'standard form contract' across all of its small business customers.

Other examples include:

- Around 1% of small business customers were able to obtain changes to one clause only of a large business's standard form contract. That change was to amend a term prohibiting the small business customer from engaging in a particular act, to a term prohibiting the small business customer from engaging in a particular act, unless it has the large business's consent.
- A large business consulted on its proposed contract with a group of its small business customers who supplied it with a premium product, in a particular state. However, it then later imposed the same contract on all its small business suppliers nation-wide, including those who supplied it with non-premium products.

It is possible that the rebuttable presumption in section 27 of the ACL may mean that it would be difficult for large businesses to use the above examples, or similar, as sufficient evidence to prove their contract is not a standard form contract. Given the lack of judicial precedent on the concept of 'an effective opportunity to negotiate' under the UCT regime, it is difficult to say how significant this issue may be.

The ACCC considers that one-off and very limited instances of consultation, negotiation or amendment should not affect the overall character of a contract as 'standard form'. If the definition of 'standard form contract' was to be interpreted in this way, it would exclude a significant number of business-to-business contracts from the operation of the UCT regime and could be easily used by parties to circumvent the UCT provisions.

To assist businesses in understanding whether their contracts are covered by the UCTs regime, the ACCC therefore recommends the ACL be amended to clarify what constitutes an "effective opportunity to negotiate". The mere fact that negligible percentage of small business customers have negotiated to obtain minor amendments to some terms in their contracts should not constitute an effective opportunity to negotiate. A business should have to show that negotiation of the contract terms is a common occurrence across its dealings with its small business customers.