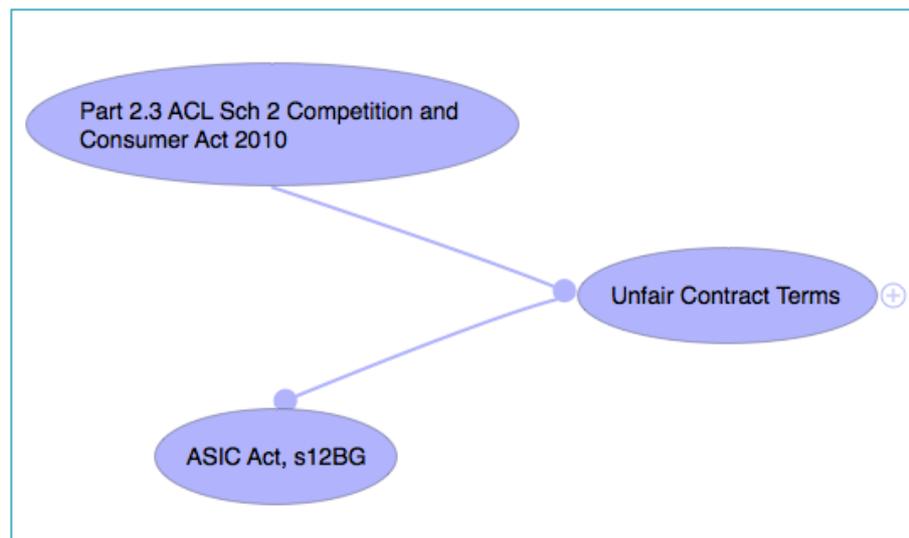


## Unfair Contracts with Small Business: The New Rules after 12 November 2016

From 12 November 2016, the **Australian Securities and Investment Commission Act 2001** (Cth) ("**ASIC Act**") will mirror the unfair contract term provisions in the **Australian Consumer Law** ("**ACL**").

The new law will protect small business from unfair contracts as consumers are currently under the ACL.



### What will the new law say?

The amendments that are mirrored in s24 of the **ACL** can be seen from the amendments to s12BF of the **ASIC Act**.

#### **S 12BF Unfair terms of consumer contracts and small business contracts**

- (1) A term of a consumer contract or small business contract is void if:
  - (a) the term is unfair; and
  - (b) the contract is a standard form contract; and
  - (c) the contract is:
    - (i) a financial product; or
    - (ii) a contract for the supply....of services that are financial services.
- (2) The contract continues to bind the parties if it is capable of operating without the unfair term.

(3) A **consumer contract** is a contract where at least one of the parties to it is an individual...(and)...what is supplied...is...for personal, domestic or household use or consumption.

(4) A contract is a **small business contract** if:

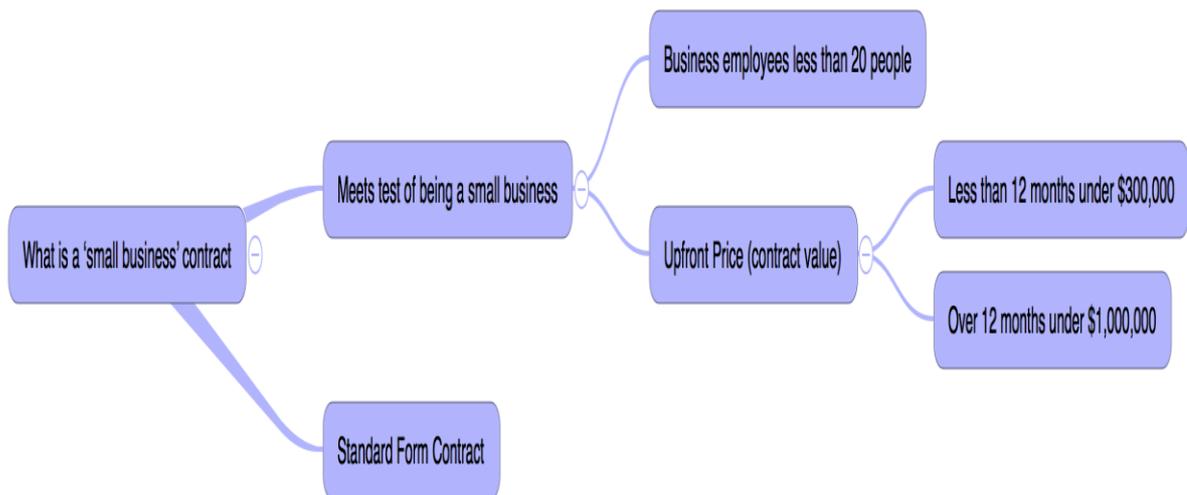
(a) ... at least one party to the contract is a business that employs fewer than 20 persons; and

(b) either of the following applies:

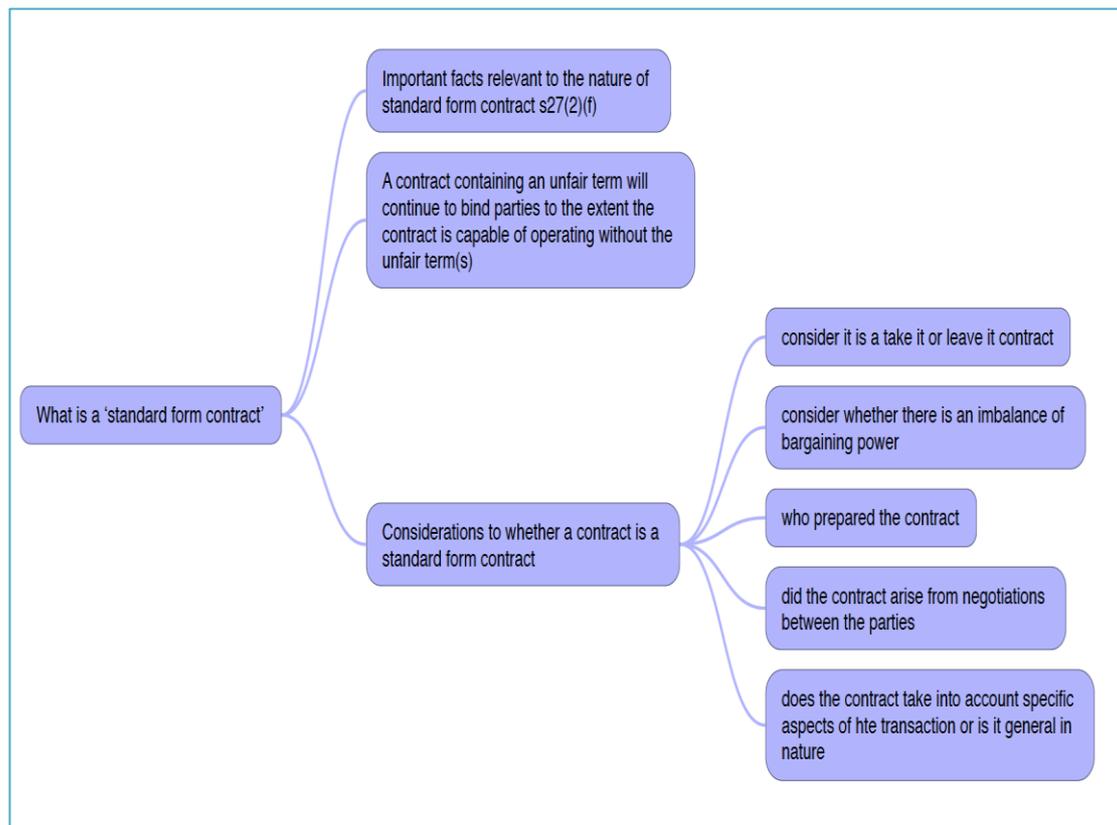
(i) the...price...does not exceed \$300,000;

(ii) the contract has a duration of more than 12 months and the...price...does not exceed \$1,000,000.

Figure 1 What is a 'small business' contract



## What is a standard form contract?



A contract is an agreement made between two or more parties that is intended to be legally enforceable.

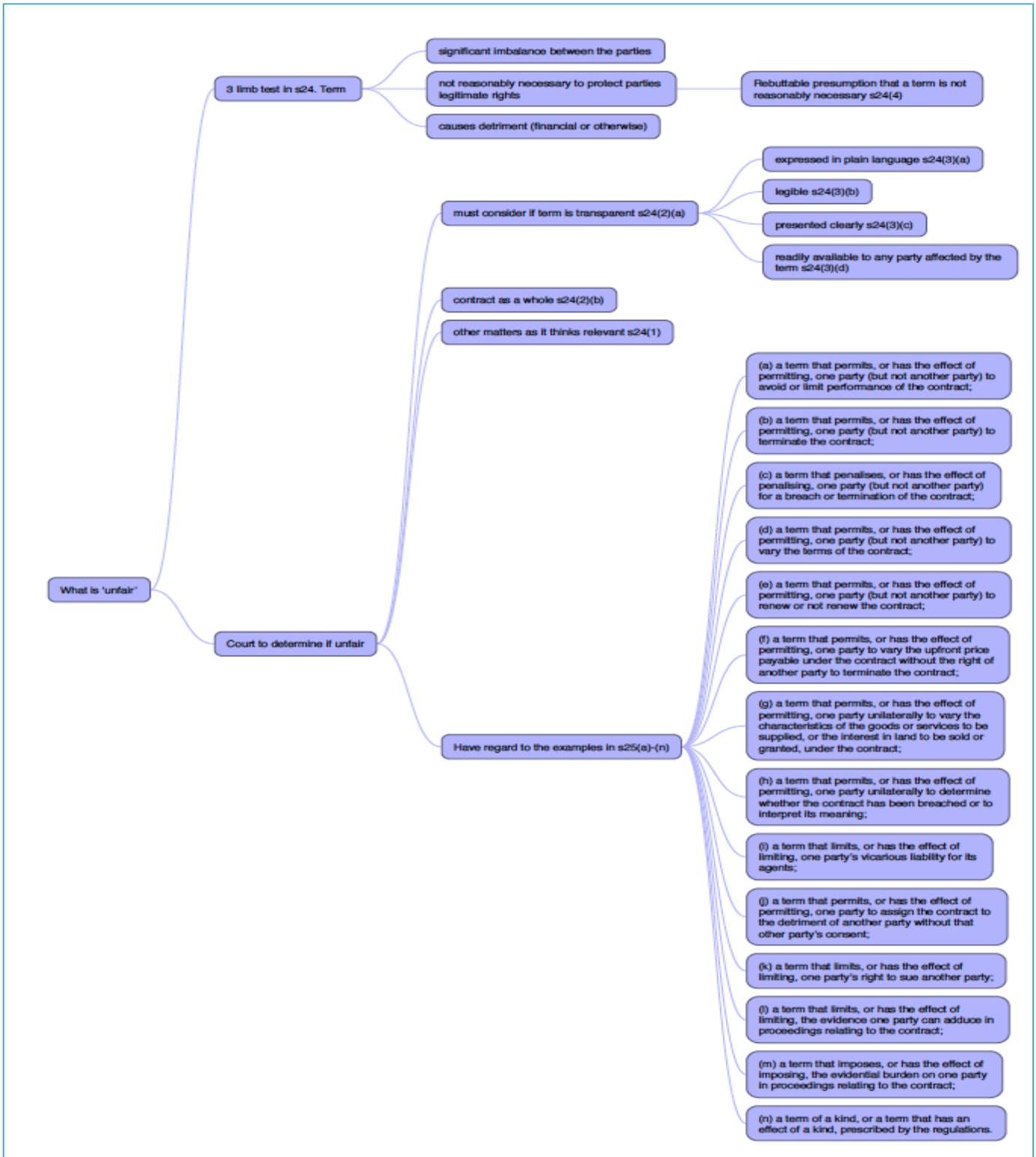
The simple, rule of thumb, is that any contract that is entered into on a “take it or leave it” basis is most likely a standard form contract.

## What is ‘unfair’?

In deciding whether a term is ‘unfair’, the court applies a three-limbed test for unfairness. A term of a contract is unfair if it:

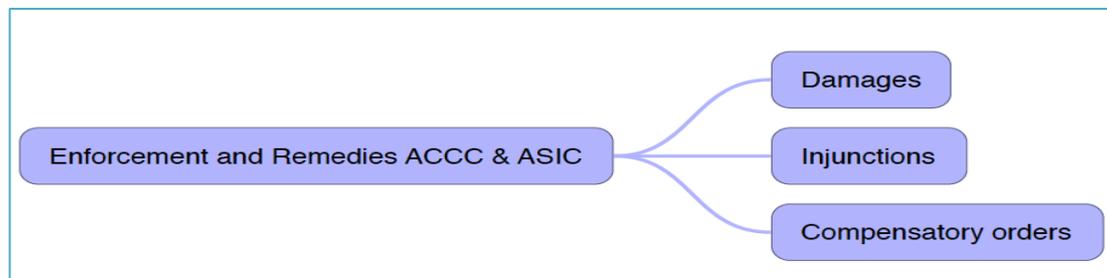
1. would cause a significant imbalance in the parties’ rights and obligations arising under the contract;
2. is not reasonably necessary to protect the legitimate interests of the party advantaged by the term; and
3. would cause detriment (financial or otherwise) to a party if it were to be relied on.

All three limbs must be proven, on the balance of probabilities, to exist for a court to decide that a term is unfair.



## The effect of an unfair term on the contract

A finding by a court that a term is unfair, thus void, means that the term is treated as if it never existed. However the contract will continue to bind the affected parties to the extent that the contract is capable of operating without the unfair term.



On ruling that a term of a contract is 'unfair' the court's powers of redress are wide. Remedies may include:

- **Disqualification orders**
- **Infringement Notices**
- **Public warning notice**
- **Injunctions**
- **Damages**
- **Any other orders the court thinks appropriate**

If you are considering drafting or challenging standard form contracts for dealings, consider the following questions:

- Variation- does one party have more power in varying the contract terms than the other?
- Indemnities- does one party (e.g. the supplier) bear no risk for breach whilst the other party bears all
- Termination- is the supplier entitled to terminate the contract without the customer having the same rights?

The amendments are significant and far-reaching. They have the potential to expose businesses to significant risk if not managed carefully.

## Your Business in the future

Work with your legal advisors to:

- Review existing standard form contracts and consider possible unfair terms; ask are the terms 'reasonably necessary'?
- Consider and document why your terms are included.
- Ensure there is an appropriate and well communicated procedure for creating and entering into standard form contracts that involve some compliance or legal review;
- Ensure staff are trained on the use of standard form contracts and potentially unfair terms.

There are still some inconsistencies within the unfair contract provisions and as a result, the new provisions are likely to become among the most litigated provisions in the **ASIC Act**. Spend some time with your legal advisors ensuring your business doesn't end up a victim.