

Productivity Commission

**INQUIRY INTO AUSTRALIA'S
CONSUMER POLICY
FRAMEWORK**

**Submission No. 2
by**

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PROMOTING FAIRER CONSUMER CONTRACTS

This second submission is concerned entirely with exploring key mechanisms for promoting fairer consumer contracts. The submission is divided into four parts, with each part intended to deliver substantial benefits to consumers. These relate to:

- Providing for “class compensation orders” as a more efficient way for affected consumers to get compensation once a regulator has proven a breach of consumer laws;
- Promote ethical business conduct towards consumers: Resuscitating and streamlining s 51AB of the *Trade Practices Act*;
- Promoting ethical business conduct towards consumers: Enacting a statutory duty of good faith; and
- Unfair contract terms.

Part 1: Class compensation order

A key challenge faced by consumers relates to their current inability to recover losses from breaches of consumer laws in a timely and cost-effective manner. All too often agencies like the ACCC can successfully prosecute breaches of the *Trade Practices Act*, but those affected by the conduct find it difficult to cost-effectively recover their losses. Within this context, it is appropriate to consider a new approach to efficiently and effectively facilitating the recovery of losses from breaches of the *Trade Practices Act* or consumer laws. Such an approach could involve giving the Courts the power to make a “class compensation order” whereby the Court would, following a finding that there has been a breach of the *Trade Practices Act* or the consumer law, order the contravening party or parties to compensate all affected parties notifying a court-appointed assessor of their loss or other claim within a specified period of time.

Under a class compensation order, the Court would have the power to compensate affected parties without the need for those parties to bring their own action or recovery proceedings. In particular, a class compensation order would, once a breach has been found in an action brought by the regulatory agency, allow the Court itself to set up a framework:

- (i) to ensure that affected parties are notified within a reasonable period of time that they are able to make a claim to the particular Court in relation to the contravening conduct;
- (ii) allowing a reasonable period of time for affected parties to lodge their claim;
- (iii) appointing an assessor, answerable to the Court, to review all claims lodged by affected parties within the specified time; and,
- (iv) for the Court to finally approve any claim recommended by the assessor.

This process would be funded by the contravening party or parties and would provide a streamlined process for dealing with individual claims arising from a proven breach. While there would be judicial oversight of the process, the Court itself would not be tied down by having to consider the factual background of each affected party. Indeed, any factual assessment of individual claims can easily be undertaken by an assessor or assessors, who could conduct such assessments in a very efficient and cost effective manner without the need to take up valuable court time.

Thus, a class compensation order would not only enable parties affected by the contravening conduct to recover their losses in a streamlined manner, but such an order would be an excellent way to avoid courts being clogged up by a proliferation of individual recovery actions which may occur at present. Importantly, a class compensation order would allow the Courts to respond flexibly and effectively to cases where a large number of parties are affected by the contravening conduct and, in this regard, the availability of a class compensation order would enable the regulatory agency to play a leadership role in targeting conduct that has a wide-ranging detrimental impact on consumers and other similarly affected parties.

My proposal for a "class compensation order" was considered on page 236 of an article published last year titled "Are Australia's consumer laws fit for purpose," (*Trade Practices Law Journal*, Vol. 15, p. 227). A copy of the article has been provided to the Commission and I would be very happy for that article to be considered a part of my Submissions to this Inquiry.

Part 2: Promoting ethical business conduct towards consumers: Resuscitating and streamlining s 51AB of the *Trade Practices Act*

The following approaches to resuscitating and streamlining s 51AB of the *Trade Practices Act* represent a variety of statutory mechanisms for promoting ethical business conduct towards consumers:

- Having just one section dealing with unconscionable conduct;
- Inserting a statutory definition of the term “unconscionable;” and
- Inserting a statutory list of examples of the types of conduct that would ordinarily be considered to be “unconscionable.”

Having just one section dealing with unconscionable conduct

During the past fifteen years there has been a proliferation of provisions dealing with unconscionable conduct. With unconscionable conduct being dealt with at the Federal level by sections 51AA, 51AB and 51AC of the *Trade Practices Act* and sections 12CA, 12CB and 12CC of *Australian Securities and Investments Commission Act 2001*, there are very strong cases for only one provision dealing with unconscionable conduct. A proposal for a single provision dealing with unconscionable conduct is provided below.

Resuscitating s 51AB by inserting a statutory definition of the term “unconscionable”

The insertion of a definition of “unconscionable” in s 51AB would be an obvious way to provide clear statutory guidance as to what is meant by the term as is used in s 51AB. Importantly, the insertion of a statutory definition in s 51AB would send a clear parliamentary signal to the Courts that the concept is not only broader than the present judicial interpretation of the concept, but that s 51AB is intended to promote ethical business conduct towards consumers. Such a definition would set out a non-exhaustive benchmark for assessing conduct to determine whether or not it goes beyond what is reasonably necessary to protect the legitimate interests of the parties involved. This would

provide clear statutory guidance as to what is considered to be unethical. Currently, in the absence of a statutory definition in 51AB of the term “unconscionable” the Courts are being left to define the term and, in doing so, are taking such an onerous view of what constitutes “unconscionable” that s 51AB is falling into disuse.

Inserting a statutory list of examples of the types of conduct that would ordinarily be considered to be “unconscionable”

An alternative to inserting a statutory definition of “unconscionable” would be to recast the existing list of factors under s 51AB to represent *examples* of conduct that would ordinarily be considered to be “unconscionable.” Currently, the factors can be considered or dismissed at the Court’s discretion and as mere factors certainly cannot be seen to define what is unconscionable. Recasting the factors into examples of unconscionable conduct would provide considerable and practical statutory guidance as to what is meant by the term “unconscionable.”

A single provision prohibiting unconscionable conduct: A proposal

The following is a draft of a single provision that could be enacted to deal with unconscionable conduct under the *Trade Practices Act*.

- (1) A corporation must not, in trade or commerce, engage in conduct that is, in all the circumstances, unconscionable.
- (2) For the purposes of this section “unconscionable conduct” includes any action in relation to a contract or to the terms of a contract that is unfair, unreasonable, harsh or oppressive, or is contrary to the concepts of fair dealing, fair-trading, fair play, good faith and good conscience.

This proposed provision has a number of noteworthy features. Firstly, the proposed provision prohibits unconscionable conduct in trade or commerce generally. This removes the current reference to the supply of goods or services in both s 51AB and s 51AC, but is in keeping with the current s 51AA. The current reference to the supply of goods or services in s 51AB and s 51AC is superfluous

and its removal would simplify the proposed provision. The drafting of a single provision prohibiting unconscionable conduct in trade or commerce generally is intended to create a new ethical norm of conduct in the same way that s 52 has established a norm of conduct within trade or commerce.

Secondly, the proposed provision incorporates a non-exhaustive definition of unconscionable conduct. This is intended to overcome the restrictive view that the Courts are currently taking towards the notion of “unconscionable conduct” under s 51AB and s 51AC. Indeed, in applying the concept of “unconscionable conduct” under s 51AB and s 51AC the Courts are focusing increasingly on procedural unconscionability. In doing so, the Courts continue to be influenced by the narrow equitable doctrine of unconscionability. While perhaps not surprising given the concept of “unconscionable conduct” has been previously used under the equitable doctrine of unconscionability, this procedural unconscionability bias unfortunately raises considerably the threshold for succeeding under the s 51AB and s 51AC. Thus, to ensure that the concept of “unconscionable conduct” in the proposed provision is given a wider application than is currently the case it would be very useful to include a legislative definition of the concept of “unconscionable conduct.” Such a definition defines “unconscionable conduct” by reference to a variety of other known concepts that make it clear that the term “unconscionable” as used under the proposed provision is one concerned with dealing with unethical conduct within trade or commerce generally.

Finally, the proposed provision does not have a monetary cap on the value of transactions covered by the proposed provision. The lack of a monetary cap can readily be supported on the basis that (i) a monetary cap may exclude some parties from the proposed provision; (ii) raises definitional regarding the application of the monetary cap; and (iii) a monetary cap can be very artificial and ultimately detracts from what should be the only issue in cases under the proposed provision; namely, whether or not the conduct is “unconscionable.”

Part 3: Promoting ethical business conduct towards consumers: Enacting a statutory duty of good faith

While any statutory definition of “unconscionable” could usefully rely on the concept of good faith as a means of ensuring the Courts take a broader approach to s 51AB than their presently onerous and very legalistic approach to the section, an alternative would be to enact a stand-alone statutory duty of good faith. Either way, the concept of good faith offers considerable potential as a mechanism for promoting ethical business conduct. Indeed, this is readily apparent from the growing judicial attention and support given to an implied duty of good faith in commercial contracts, especially in New South Wales.¹

A convenient summary of the nature and scope of an implied duty of good faith was recently provided by Gordon J in *Jobern Pty Ltd v BreakFree Resorts (Victoria) Pty Ltd*.²

146 Specific conduct has also been identified by various courts as constituting ‘*bad faith*’ or a lack of ‘*good faith*’ including:

- (1) acting arbitrarily, capriciously, unreasonably or recklessly: e.g. see Viscount Radcliffe in *Selkirk v Romar Investments Ltd* [1963] 1 WLR 1415 at 1422-23 cited by Gyles J in *Goldspar* at [173]; and *Pacific Brands Sport & Leisure Pty Ltd v Underworks Pty Ltd* [2005] FCA 288 at [65];
- (2) acting in a manner that is oppressive or unfair in its result by, for example, seeking to prevent the performance of the contract or to withhold its benefits: *Pacific Brands Sport & Leisure Pty Ltd v Underworks Pty Ltd* [2005] FCA 288 at [65]-[66];
- (3) failing to have reasonable regards to the other party’s interests: *Overlook Management BV v Foxtel Management Pty Ltd* (2002) ACR 90–143 at [67] ...
- (4) failing to act ‘reasonably’ in general. ...

¹ See for example *Renard Constructions (ME) Pty Limited v Minister for Public Works* (1992) 26 NSWLR 234; *Alcatel Australia Limited v Scarcella* [1998] NSWSC 483 (16 July 1998); *Burger King Corporation v Hungry Jack’s Pty Limited* [2001] NSWCA 187; *Overlook v Foxtel* [2002] NSWSC 17 (31 January 2002); and *Vodafone Pacific Ltd & Ors v Mobile Innovations Ltd* [2004] NSWCA 15 (20 February 2004).

² [2007] FCA 1066 (23 July 2007).

Clearly, the concept of good faith has not only received strong judicial support, but now has reached the point in Australia where its nature and scope is being defined with an increasing degree of precision. Consequently, there is a ready body of law on which a statutory duty of good faith could quite readily and usefully draw upon in seeking to promote ethical business conduct.

Part 4: Unfair contract terms

With all due respect, a number of propositions put forward in the Draft Report in relation to unfair contract terms are questionable. Some propositions are judgemental and others appear more concerned with protecting businesses than consumers. For example, the focus on “opportunistic” consumers to justify “vague disclaimers” is troubling as it appears to be justifying the use of unfair contract terms which allow businesses considerable discretion on how they deal with a consumer that the business considers to be “opportunistic.” Does this mean that if a business thinks a consumer is “nice” then the unfair term won’t be used aggressively or won’t be used as aggressively as it would be used against an “opportunistic” consumer? This sounds judgmental and shifts the policy focus onto how we protect the business as opposed to how we promote fairer consumer contracts. This seems to indicate a policy stance more concerned with protecting a business than dealing with unfair contract terms.

Surely, the appropriate policy stance should be to ask whether or not there are unfair contract terms and, if so, how do we deal with them in an efficient manner. It is the existence of unfair contract terms that is the problem; not whether or not the business is nice enough not to use it against the bulk of consumers or whether a business only uses the term when it thinks the consumer is behaving opportunistically. Clearly, the mere existence of unfair contract terms is the problem that needs to be addressed in the first place. Once that problem is addressed, then the further problem of the potential use of unfair contract terms will also necessarily be addressed. To seek to address only the problem of the subsequent use of an unfair contract term is inefficient as it only deals with a symptom and not the cause of the real and underlying problem which is the existence of the unfair contract term in the first place.

In any event, as an unfair contract term is one that goes beyond what is reasonably necessary to protect the legitimate interests, it is clear that the legitimate interests of the business are already amply protected under legislation dealing with unfair contract terms. With the exception of Victoria, what is currently not being dealt with in Australia is the practice by which businesses seek to insert contract terms that go beyond what is reasonably necessary to protect the business’s interests. By necessary implication this

means that businesses are being allowed to shift contractual risks disproportionately onto consumers.

The draft report talks freely of “opportunistic” consumers, but doesn’t talk about “opportunistic” businesses which hide behind unfair contract terms to disadvantage consumers. There is no talk of “opportunistic” businesses abusing their contractual power to shift contractual risks disproportionately onto consumers. Legislation dealing with unfair contract terms is not about picking sides or being judgemental, but rather such legislation is concerned with providing a framework for promoting fairer consumer contract and for promoting efficient markets for the provision of goods or services for the benefit of consumers.

As for the operation of legislation dealing with unfair contract terms, the draft report downplays the evidence of savings or benefits already achieved by that legislation in the United Kingdom and Victoria, while overstating the potential costs of the legislation. Unfortunately, the draft report understates the benefits of legislation dealing with unfair contract terms in a number of ways:

- (i) there are considerable benefits where cases are resolved through consultation rather than litigation. There have only been less than a handful of cases in both the United Kingdom and Victoria, even though the United Kingdom framework has been operating for over 10 years. This saves court time and also saves businesses, consumers and regulatory agencies the considerable costs associated with litigation;
- (ii) There also considerable benefits associated with negotiated settlements, which are the norm in relation to unfair contract terms legislation. This is because of the clear benchmarks in the unfair contracts legislation regarding what is “unfair” under the legislation. The Regulator and the affected business have a known set of legislative criteria to apply, thereby facilitating a negotiated settlement. This saves times and minimises the potential for disagreement;
- (iii) The timely resolution of concerns regarding an allegedly unfair term under legislation dealing with unfair contracts is a considerable benefit in itself. One is reminded of the adage that “justice delayed is justice denied.” Timely resolution of concerns builds consumer confidence with for example, the use of standard form contracts;

- (iv) There are considerable benefits to allowing consumers and regulatory agencies to challenge allegedly unfair terms on the basis that such action seeks to correct the significant market failure associated with those terms being offered on a `take it or leave it' basis. As allegedly unfair terms may be standard within the industry and/or there is no competition regarding those terms, the market is not delivering efficient outcomes that maximise the welfare of consumers;
- (v) Having legislation dealing with unfair contracts has a deterrent effect on businesses planning to exploit the market failure surrounding the absence of competition in relation to most contract terms. This deterrent effect is beneficial in helping promote efficient outcomes that maximise the welfare of consumers.

In relation to costs of legislation dealing with unfair contract terms, it is troubling to see comments like those on page 122 of Volume 2 of the draft report:

“A reduced capacity for businesses to impose some contingent charges on consumers, such as certain termination fees, would lower businesses' profits because their revenues, but not their costs, would have fallen. As noted above, this could be expected to place upward pressure on upfront prices, thus reducing the gains to consumers from acting on unfair terms.”

The maintenance of business profits is not and should not be a relevant consumer policy objective. Consumer policy is concerned with maximising consumer welfare within the context of an efficient and competitive market place. As for whether a business is able to charge a particular fee, the question is *not* whether the charge is necessary to maintain the profits of the business, but rather whether the charge the business is imposing is reasonably necessary to protect the legitimate interests of the business in supplying the goods or services.

In any event, if there was any “upward pressure on upfront prices” because an unfair contract term was reworded or deleted, then the consumer may have the ability to walk away. Consumers can't walk away once they are locked into a contract with unfair contract terms. Also, there is a greater likelihood of competition between competitors on the upfront price. While there is unlikely to be

competition in relation to the vast bulk of contract terms, there may be competition in relation to upfront fees. Again, legislation dealing with unfair contract terms is not about picking winners, but rather is intended to promote fairer consumer contracts and the efficient operation of markets for the provision of goods or services for the benefit of consumers.

The role of the regulator is also subject to unnecessary negative comment. On page 122 of Vol 2 of the draft report states that:

“There are also concerns that regulators might be overly zealous in interpreting the term.”

Such comments are also judgemental as a business faced with inquiries from the regulator is quite likely to be defensive. Possible concerns of how a regulator may or may approach their role under legislation dealing with unfair contract terms should not be used to deny consumers the benefits of such legislation or to justify drafting the legislation in very restrictive terms as being proposed by the Commission. Don't shoot the messenger, if the term is questionable then the business can arrive at a negotiated settlement with the regulator. There is ample evidence that this approach has worked in all but a few cases in the United Kingdom and Victoria. Of course, if businesses feel that a regulator is being “over zealous” then they can have the matter tested by a court or a Tribunal as happens in Victoria.

Importantly, the Commission is not able to point any evidence of that the United Kingdom or Victorian legislation dealing with unfair contract has imposed any major costs on businesses. On page 122 of Vol. 2 of the draft report the Commission states:

“Notably, business has not identified major costs associated with the introduction of unfair contract laws in Europe, the UK and Victoria.”

This is a critical finding that provides further evidence that the concerns or costs of legislation dealing with unfair terms are being significantly overstated by the Commission.

Any overstating of the costs or understating of the benefits of legislation dealing with unfair contract terms is of concern as it may result in a distorted view of such legislation to the detriment of consumers. We need to remember that the legislation in Victoria

and the United Kingdom has resulted in the rewriting or deletion of unfair contract terms and has done so in a way that has not undermined consumer contracts or imposed major costs on businesses.

In short, while there are no obvious problems with how the United Kingdom or Victorian legislation is operating, there is growing evidence that the United Kingdom and Victorian legislation is delivering real benefits to consumers and even businesses. Indeed, the UK National Audit Office pointed to evidence on page 53 of the 1999 Report entitled *The Office of Fair Trading: Protecting the Consumer from Unfair Trading Practices* that:

“One mobile phone company told us that they expected the revised contract to make their services more attractive to consumers.”

The Victorian legislation has already led to a beneficial re-writing of mobile phone contracts with general industry wide support, a point I made in my evidence to the Commission at last year’s public hearing in Sydney.

In this environment, it is surprising that the Commission is recommending a new and very restrictive approach to unfair contract terms. This new approach brings uncertainty. The Commission’s recommended provision to deal with unfair contract terms is novel and inconsistent in key aspects with the United Kingdom and Victorian legislation. This in itself would impose regulatory costs on business and deny consumers the full benefits available under the United Kingdom and Victorian legislation.

The Commission’s requirement to confine actions by the regulator under its recommended provision to instances where a consumer (or consumers) had already suffered material detriment from an unfair term is extremely onerous and generally not required of a regulator. A requirement for a regulator to show material detriment to a consumer as a pre-condition of bringing enforcement action is generally out of step with accepted approaches to consumer law and its enforcement. The regulator under the United Kingdom and Victorian legislation is enforcing a public policy objective. That public policy objective is to promote fairer consumer contracts by seeking to prevent the inclusion of unfair terms in consumer contracts in the first place. The recovery of a loss arising from a

breach of that public policy objective, however, is a different matter and that requires proof of detriment.

In short, a regulator is not generally required to show actual or material detriment or loss as a pre-condition for enforcing consumer laws because the disadvantage to consumers generally from the non-adherence with the consumer law by businesses may be broader than the actual loss suffered by an individual consumer. Thus, the disadvantage to consumers in general may be the inefficient operation of a market or unethical behaviour being engaged in by rogue businesses. Importantly, it is the attempt by Parliament to remove that disadvantage that is the public benefit that Parliament is seeking to achieve.

Indeed, consumer laws are typically concerned with establishing norms of conduct that Parliament requires businesses to adhere to when dealing with consumers. Having established the norm of conduct, Parliament expects it to be adhered to in its own right as an appropriate standard of conduct. That is the public benefit or policy objective that Parliament is seeking to achieve. The establishment of the norm of conduct is a matter of public policy to be enforced by the regulator and the recovery of any loss from a breach of that norm is a matter for an individual consumer on proof of actual loss.

Overall, it would be submitted that the Victorian framework should be the basis of a national framework for dealing with unfair terms in consumer contracts. Such a national framework can build on the excellent work already done by Consumer Affairs Victoria. Of course, there could be additional features introduced into a national framework for dealing with unfair contract terms and these are discussed in the various articles I have published in the area. These include: (i) Zumbo, F., (2007), "Promoting Fairer Consumer Contracts: Lessons from the United Kingdom and Victoria," *Trade Practices Law Journal*, Vol. 15, pp. 84-95; (ii) Zumbo, F., (2005), "Dealing with Unfair Terms in Consumer Contracts: The search for a new regulatory model," *Trade Practices Law Journal*, Vol. 13, pp. 194-213; (iii) Zumbo, F., (2005), "Dealing with Unfair Terms in Consumer Contracts: Is Australia Falling Behind?" *Trade Practices Law Journal*, Vol. 13, pp. 70-89. A copy of these articles has been provided to the Commission and I would be very happy for them to be considered a part of my Submissions to this Inquiry.