



---

## EXTENDING UNFAIR CONTRACT TERM PROTECTIONS TO SMALL BUSINESSES



August 2014

---

# CONTENTS

---

## Table of Contents

<b>Insurance Australia Group .....</b>	<b>3</b>
<b>Executive summary .....</b>	<b>4</b>
<b>Introduction .....</b>	<b>5</b>
<b>The use of Standard Form Contracts .....</b>	<b>6</b>
<b>Small Business and IAG – serving a mutual customer .....</b>	<b>7</b>
<b>A model of success: Partnering with small business .....</b>	<b>8</b>
About the NRMA Insurance Partner Repairer Model.....	8
<b>Frameworks of fairness .....</b>	<b>10</b>
<b>Power to negotiate.....</b>	<b>11</b>
<b>What is ‘unfair’?.....</b>	<b>12</b>
<b>Targeted reform .....</b>	<b>13</b>
<b>The scope of protections .....</b>	<b>14</b>
Defining small business.....	14
<b>Current Protections and Industry Led Initiatives .....</b>	<b>15</b>
MVIRI Code of Conduct .....	15
Small Business Commissioner .....	16
<b>Dispute mechanism considerations .....</b>	<b>17</b>
<b>Sanctity of Contract must remain paramount .....</b>	<b>18</b>
<b>Education and Guidance.....</b>	<b>19</b>
<b>Unfair contract terms in general insurance contracts versus supply of goods or services .....</b>	<b>20</b>

Cover image: (c) agencyby [www.fotosearch.com](http://www.fotosearch.com) Stock Photography

---

# INSURANCE AUSTRALIA GROUP

---

Insurance Australia Group (IAG) welcomes the opportunity to respond to the 'Extending Unfair Contract Term Protections to Small Businesses' Consultation Paper.

IAG is the parent company of a general insurance group with controlled operations in Australia, New Zealand, Thailand and Vietnam, employing more than 15,000 people.

Its businesses underwrite over \$11 billion of premium per annum, selling insurance under many leading brands, including: NRMA Insurance, CGU, SGIO, SGIC, Swann, WFI and Lumley Insurance (Australia); NZI, State, AMI and Lumley Insurance (New Zealand); Safety and NZI (Thailand); and AAA Assurance (Vietnam). IAG also has interests in general insurance joint ventures in Malaysia, India and China. IAG has more than 762,000 shareholders and share register is the fourth largest in Australia.

Across its portfolio of brands IAG insures 8.4 million cars, 2.9 million homes, 103,000 farms, 123,000 employers and 408,900 businesses.

---

# EXECUTIVE SUMMARY

---

IAG supports the principle of protecting small business from unfair contract terms including extending legislative protections where necessary. However, in our experience, an open process and an approach of fairness and transparency in dealing with small businesses is just as important as ensuring fair terms within a contract itself.

IAG depends on the many and varied partnerships we have in place with small business. While we utilise standard form contracts due to the range of benefits they offer small and large business, we believe there is no place in standard form contracts for one-sided terms that go beyond the legitimate business interests of a contracting party and are unfair.

We cannot meet the promises we make to our customers without small businesses and our approach to working together is one of collaboration, mutual respect, fairness and sustainability.

No more so is this true than in our approach to working with the smash repair industry. Five years ago IAG's Personal Insurance, the division behind the NRMA Insurance brand, evaluated a number of strategic options to enable it to remain competitive in an increasingly crowded and price-driven comprehensive motor vehicle insurance market.

Among the options was to follow the path of IAG's major competitor and own and operate smash repair shops. This option was quickly dismissed based on two key factors: the first outcome-based, the second on a commitment to supporting the sustainability of an industry upon which NRMA Insurance has relied for over 85 years.

NRMA Insurance quickly concluded that its strengths lie in knowing insurance exceptionally well and having a long-standing history of being there when people need us most. We are not the experts in the profession of repairing modern day motor vehicles and believe that task should be placed in the hands of highly skilled and innovative small business people who dedicate their career to performing quality repairs and delivering great customer service.

It is with these businesses that we have formed long term partnerships underpinned by a variety of commercial contracts tailored to each repairer and founded on terms proposed by the repairers themselves.

These partnerships are a model of success and we have applied the positive response to these contracts to expand the model across our broader supply chain.

We look forward to continuing our work to lead positive evolution and development in the smash repair industry and to sharing our experiences with other small businesses - and with government - of the benefits that come from a partnership approach.

---

# INTRODUCTION

---

In preparing this response, IAG has commissioned an external review of its major supplier contracts. We are confident our contracts are fair and help ensure the sustainability of industries we depend upon to meet the promises we make to our customers when they purchase their insurance.

IAG supports in principle the extension of the Unfair Contract Terms to small business. We believe there is no place in contracts for one-sided contract terms that go beyond protecting the legitimate business interests of one party and are unfair.

While supporting the extension of the unfair contract terms to small businesses, we believe consideration should also be given to the alternatives to a broad based extension of unfair contract terms legislation. This could include reform targeted to industries where there exists well documented evidence of unfair terms and a 'take it or leave it approach' from larger business.

---

# THE USE OF STANDARD FORM CONTRACTS

---

Various standard form contracts are used across our business.

These contracts are used in our business dealings with small and large businesses alike and bring a range of advantages and benefits to both contracting parties including:

- **Expense:** Standard form contracts reduce transaction time and costs. It is expensive and time consuming to frequently draft new agreements with suppliers, especially when the services provided by these suppliers are similar.
- **Certainty for both parties:** Standard form contracts used by IAG provide certainty and understanding between parties as they are usually quite extensive. Many of the clauses included in our standard form contracts are never relied upon (eg. dispute resolution or termination clauses), yet these can assist in the business relationship as the obligations and expectations are clearly articulated within the agreement.
- **Convenience:** Similarly, standard form contracts are convenient, particularly for larger organisations, as employees and managers can better understand their legal position across a variety of agreements or arrangements they may have with other organisations if the important and key terms of these contracts are the same or similar.

Of course, standard form contracts must be fair and reasonable to the extent that they should not include terms that are not reasonably necessary to protect the legitimate business interests of a party, cause detriment to the other party to the contract and are unfair.

---

# SMALL BUSINESS AND IAG - SERVING A MUTUAL CUSTOMER

---

IAG and its subsidiary companies rely on the services of thousands of small businesses every day.

Across our vast and varied supply chain (including motor, home and commercial portfolios) we pursue a strategy which creates long-term, equitable partnering arrangements with small business.

This commitment to partnering is used and promoted each day in all facets of our business, from glass suppliers, home contents restorers and suppliers, to builders and smash repairers.

This series of partnering arrangements helps to deliver a high quality product and service to our customers, while at the same time supporting and growing local and regional small businesses.

These partnerships help ensure we remain competitive: the positive experience we can provide to a customer when they need to make an insurance claim differentiates us and our suppliers from our competitors.

---

# A MODEL OF SUCCESS: PARTNERING WITH SMALL BUSINESS

---

Our approach to partnering with small business is best exemplified by the experiences our customers and Partner Smash Repairers have with the NRMA Insurance Partner Repairer model.

This approach provides a working example of how a business model based on partnering with small business for mutual benefit (as opposed to a relationship purely based on the written contract or application of unfair contract terms) achieves a successful and sustainable outcome for large and small business.

## About the NRMA Insurance Partner Repairer Model

NRMA Insurance Partner Repairers are a team of independent small businesses who share our values of integrity, quality and focus on ensuring a great outcome for our customers.

A vital part of helping to ensure great outcomes for our customers is the nature of the contracts underpinning these small business relationships, and the process that was undertaken prior to a single contract being signed.

Our Partner Repairer model was established via an open, fair and rigorous Request for Proposal (RFP) process that every repairer nationally in the markets where we operate (NSW, ACT, VIC, WA, and QLD) had an opportunity to take part in.

The approach was designed to ask repairers how they wanted to work with us, and moreover to give us the opportunity to assess each participating repairer's capability to deliver high quality repairs consistent with manufacturer's standards. At the time of the RFP it was made clear that any repairer who chose not to participate in the RFP would not be considered for a position in our new network.

All repairers who lodged a submission to the RFP received visits to their premises by our evaluation team. The purpose of the visits were two-fold: it gave repairers an opportunity to showcase their businesses and supplement the information they had provided in their written submissions; and secondly, it gave our team an opportunity to critically assess first-hand the customer service and quality processes of the repairer, and the technology, equipment and resources each repairer could offer to correctly (and safely) repair our customers' cars.

Repairers were then rated on these attributes, as well as their desire to have a strategic relationship with NRMA Insurance, and our geographical need for the number of Partner repairers required in each area based on the volume of repairs available. A short-list of candidates was formed and it was only at this stage that commercial discussions were held with the short-listed repairers.

Successful RFP repairers were requested to state their preference on the length of the contract they would be offered (typically 3 – 5 years) given the different circumstances and conditions relating to each repair business. All successful repairers requested a 5-year contract term as it allowed them to plan and obtain the necessary finance to be able to invest in their business with a greater level of certainty. Given the increasing complexity of repairing the modern day car, this investment is crucial in ensuring repairers have the right training and the latest equipment to enable them to repair cars safely.

Because of the value and length of the contracts, the small businesses we partner with generally engaged legal services prior to signing a contract. This is particularly true for the exclusive arrangements (where the repairer only performs insurance work for us) we have in place with several businesses.



---

# A MODEL OF SUCCESS: PARTNERING WITH SMALL BUSINESS (CONTINUED)

---

Our network has been formed to recognise the need for specialisation: some repairers submitted proposals to only undertake repairs for driveable repairs, others wanted towed repairs, while some wanted to specialise in the prestige segment. Where possible we established relationships with our Partners that aligned to the segment specialisation they wanted.

NRMA Insurance and its Partner Repairers mutually agreed a variety of commercial contracts tailored to each repairer.

While our contracts are largely in a 'standard form', key elements of the contract were negotiated with the repairer, including volume, type of work and how much a repairer feels they need to charge to be a profitable business.

It is important to note that low cost offers made by repairers as part of the RFP we ran were rejected where we did not believe the cost proposed was sufficient for a repairer to deliver a quality repair and remain profitable. It is not in our interests to accept proposals that we believe will inevitably fail nor is it in the interest of that small business.

As a result of this process and approach - which in our experience is as important as the terms of the actual contracts - our Partners feel comfortable raising and resolving any contractual concerns directly with us.

The reality of our relationships and the processes that preceded them mean IAG and its Partners have not – and are unlikely to in the future – resort to disputing or contesting contracts on the basis of unfair terms.

This process is consistent across our supply chain. Our approach of fairness, due process and appointment based on merit is why suppliers - be they glaziers, home builders, home contents suppliers or smash repairers – want to work for, and favour us over our competitors.

---

# FRAMEWORKS OF FAIRNESS

---

Small businesses that frequently interact with larger businesses should be supported by internal systems and processes to help resolve a concern or dispute.

When it comes to our work with smash repairers, a governance structure is in place to address both the concerns from the small business operator and the customers they serve. This includes processes to provide small businesses with:

- A dedicated Relationship Manager appointed to work directly with the small business to discuss and validate concerns;
- Opportunities to produce business plans to address contractual breaches;
- Programs to support the quality of the small business's output such as our Quality Framework;
- Programs to support customer service improvement;
- Reviewing agreed commercial benchmarks and
- Independently appointed internal panels to review the status of business relationships.

We are also bound by the Motor Vehicle Insurance and Repair Industry (MVIRI) Code of Conduct which contains a number of clauses designed to provide protection for both insurer-network and non-network smash repairers.

Only after great effort and investment would we take the difficult decision to end our Partner relationship with a small business.

These are decisions made in the interest of ensuring great customer outcomes, while recognising it is unfair to other small businesses to continue to support a business that is unable or unwilling to meet its commitments, or help itself.

In rare instances where a contract needs to be terminated, in addition to the above processes it is a decision largely supported by a period of wind-down to assist the small business in its transition to alternative arrangements.

---

# POWER TO NEGOTIATE

---

When considering the current state of the smash repair industry, there is a vast divide between repairers who have invested in their businesses to meet rapidly advancing standards and those who have not. As a result repairers who have built a competitive advantage have significant powers of negotiation in commercial discussions with insurers.

Because of the complexity of repairing cars in this day and age, the barriers to entry in the smash repair industry are increasing and the number of repairers capable of delivering high quality standards is rapidly reducing.

The repairers we work with are entrepreneurial business people who have invested in their businesses and are uniquely geographically situated to serve our customer base.

As a result they are highly desirable Partners for us to work with and, with continuing consolidation in the smash repair industry, we expect their desirability to grow.

---

# WHAT IS 'UNFAIR'?

---

A recent NSW State Government Inquiry in to the motor repair industry heard an allegation from one misinformed industry stakeholder that elements of NRMA Insurance's contracts with repairers were 'unfair'.

The allegation was made by an industry body that typically represents smash repairers who are **not** part of an insurer network scheme, and who do not support insurer networks.

Specifically, allegations were made by those with whom we do not have a Partner relationship that our contracts were based on 'fixed cost' terms and that this resulted in poor quality repairs.

Such allegations were predictably from those with whom we do not have a Partner relationship.

Given the terms of our contracts were proposed by repairers themselves, are not based on a fixed cost, and that the quality of the work produced by the small businesses we partner with is of significantly higher quality (three times better) than those outside our network, the allegations are baseless and misleading.

Importantly the Committee that looked at the allegations, including copies of our actual contracts, made no recommendation to alter our contracts or our supplier model in any way.

---

# TARGETED REFORM

---

In preparing this response, IAG has commissioned an external review of its major supplier contracts.

We are confident our contracts are fair and help ensure the sustainability of industries we depend upon to meet the promises we make to our customers when they purchase their insurance.

While IAG supports the principles of extending unfair contract term protections to small business, an alternative to a broad based extension of unfair contract terms legislation could be reform targeted to industries where there exists well documented evidence of unfair terms and a 'take it or leave it approach' from larger business.

In making this point, we acknowledge that in certain industries standard form contracts may unfairly disadvantage small businesses, particularly in the absence of strong business relationships and industry codes.

---

# THE SCOPE OF THE PROTECTIONS

---

We remain committed to small business and supporting an independent and sustainable smash repair industry. We cannot however have a long term contract with every smash repairer in Australia.

As a further demonstration of our commitment to support, and not overrun, small business, we continue to work on a daily basis with the majority of repairers nationally through our stated policy of offering all customers choice of repairer. This includes authorising repairs with repairers not in our network via standard form contracts. With these high frequency transactions standard form contracts are particularly beneficial.

Despite being standard form, these contracts allow negotiation via an insurance assessor and given the fact that we provide a lifetime warranty to our customers on the overwhelming majority of these repairs the contracts do not allocate disproportionate risk on these small businesses.

Terms of these contracts are rarely disputed. However disputes can arise over what is deemed a 'fair and reasonable' cost to repair a vehicle. This is particularly true in a repair shop that is not supported by modern day processes and equipment, is not sufficiently business focussed to be able to compete with other repairers and/or receives low volumes of repair work and looks to maximise the profit margin on every repair job.

In our view matters of cost should remain outside the scope of what can be raised as 'unfair' in a dispute.

## Defining small business

We agree that, in defining 'small business' for the purpose of the unfair contract term provisions, the definition should balance businesses being able to readily identify whether or not the unfair contract provisions should apply to a particular contract, as well as what businesses are likely to benefit most from the extension of the UCT provisions.

We support a definition of 'small business' defined on the basis of annual turnover. Specifically, adoption of the definition of small business used by the Australian Taxation Office (that a small business be defined as an entity with annual turnover of \$2 million or less). This is the most appropriate options of those outlined in the consultation paper, as a definition based on turnover provides a good indication of the resources available to a business to review their contracts and agreements and their ability to manage risk.

As the consultation paper identifies the problems associated with standard form contracts and unfair contract terms relate to lack of resources. As such we oppose any definition of small business that is defined on the basis of a transaction threshold. In practice this option would involve the provisions applying to large, significantly resourced businesses, as well as smaller businesses.

Similarly, extending the scope of the provisions to all business to business contracts other than those between publically listed companies has similar overreach that would extend the scope of the provisions beyond what is required to address the problem identified.

---

# CURRENT PROTECTIONS AND INDUSTRY LED INITIATIVES

---

When it comes to smash repairers, several avenues and frameworks are in place to protect these small businesses.

These protections however cannot remove the pressures that market “supply and demand” factors place on repairers’ abilities to run sustainable businesses, nor can the extension of the proposed protections provide a solution to addressing all issues and challenges within the industry.

## **MVIRI Code of Conduct**

The insurance and motor vehicle repair industry operate under a business-to-business code of conduct called the Motor Vehicle Insurance and Repair Industry (MVIRI) Code of Conduct.

The MVIRI Code provides minimum, industry wide standards including:

- Transparency, disclosure and fairness in relation to insurer’s smash repairer schemes;
- Transparency, disclosure and fairness in relation to quotation processes, times and rates of pay, repairer choice and use of parts;
- Responsibility for quality and safety and warranties;
- Minimum terms of payment;
- An independent external dispute resolution mechanism.

The MVIRI Code is intended to promote transparent, informed, effective and co-operative relationships between smash repairers and insurance companies based on mutual respect and open communication. Insurers and Repairers agree to observe high standards of honesty, integrity and good faith. The Code will specify standards of fair-trading, process and transparency in the relationship between Insurers and Repairers.

The Code was introduced at a time when relationships between insurers and repairers required significant improvement and the Code was viewed as a major way forward.

In terms of measuring the effectiveness of the Code in regulating relationships between repairers and insurers, it has been one important pathway to improved relationships in an environment of consistent industry change and remains relevant.

We continue to support the industry Code of Conduct, although the reality of our modern and mature business partnerships with our own Partner network makes the Code largely redundant in terms of the majority of our business dealings with the industry on a day-to-day basis.

Nonetheless, clauses within the Code relating to repairers rights in an insurer network scheme (particularly in relation to transparency, disclosure and fairness) affords repairers adequate protection should a dispute arise.

We submitted an extensive response to the MVIRI Code of Conduct Review 2013.

We strongly believe that any proposed amendments to the Code must not impede or restrict the fair, reasonable and mutually beneficial commercial relationships which exist between individual insurers and repairers. This was a fundamental principle of the Code’s establishment.

---

# CURRENT PROTECTIONS AND INDUSTRY LED INITIATIVES (CONTINUED)

---

## **Small Business Commissioner**

The NSW Small Business Commission hears matters regarding contractual disputes. Our interactions with the Office of the Small Business Commissioner are rare and have never related to terms within our contracts.



---

# DISPUTE MECHANISM CONSIDERATIONS

---

IAG cautions against creating 'dispute shopping lists' for small business by which a small business, supported by their industry association, access every dispute resolution mechanism possible with the intent of chewing up time and resources of the other party, rather than seeking to resolve the matter of a small business that may consider itself to have been unfairly disadvantaged.

Seemingly never ending options for dispute, coupled with an overly onerous compliance regime, acts only as an incentive for large businesses to vertically integrate the services provided by small business partners.

---

# SANCTITY OF CONTRACT MUST REMAIN PARAMOUNT

---

As the discussion paper rightly states it is essential that any extension of the UCT provisions maintains the 'sanctity of contract' to the maximum extent possible. Provisions that provide for contractual terms to be struck out potentially threaten the principle of 'sanctity of contract' and may undermine the degree of certainty and business efficiency that standard form contracts provide.

We urge caution against the unfair contract term provisions providing a forum for misconceived or unmeritorious actions to strike out terms that are inconvenient as opposed to be genuinely unfair.

We also note that disputes must not impede the need to provide the outcomes our customers expect.

Business certainty and sanctity of contracts is vital and determination of whether a term is unfair, and thus void, should be made only by a court as is currently the case with the existing consumer unfair contract terms provisions.

To ensure that 'sanctity of contract', and confidence in entering into contractual arrangements with small business any extension of the UCT terms to small business should include the following features:

## **Provisions must be Clear and Unambiguous**

Any extension of the Unfair Contract Terms provisions must be drafted in terms that are clear and unambiguous to provide certainty to all parties as to the application of the laws from the outset of contract formation.

## **Three Limbed Test:**

The current three limbed test to what amounts to an 'unfair' contract term in the Australian Consumer Law should also apply to small business.

## **What is 'unfair' should be determined by a court**

As is the case with the consumer unfair contract terms provisions in the Australian Consumer Law, given the importance of maintaining sanctity of contract, and the various factors and circumstances that must be considered, a court is and must remain the only decision making body that can make a determination that a term of a contract is unfair.

---

# EDUCATION AND GUIDANCE

---

IAG recommends that the introduction of the protections be supported by a comprehensive and targeted education campaign to assist small business in accessing the most suitable code, law or framework to have a dispute heard.

This should be supported by guidance to small and large business on what terms would be perceived as unfair.

---

# UNFAIR CONTRACT TERMS IN GENERAL INSURANCE CONTRACTS VERSUS SUPPLY OF GOODS OR SERVICES

---

Small businesses are currently protected by the Insurance Contracts Act 1984 (Cth) (IC Act), supplemented by other laws such as the Corporations Act 2001 Cth (Corporations Act) and ASIC Act 2001 (Cth) (ASIC Act) in relation to general insurance purchases. These laws collectively provide equivalent, if not greater, protections to small businesses from unfair contract terms in relation to insurance they purchase.

IAG submits that the existing exemption under section 15 of the IC Act for insurance contracts from the operation of unfair contract term legislation should be retained in its entirety.