



**Small Business Development Corporation**

**Extending Unfair Contract Term Provisions to Small  
Businesses**

**August 2014**



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Development Corporation**

## **About the Small Business Development Corporation**

The Small Business Development Corporation (“SBDC”) welcomes the opportunity to provide this submission to the Federal Treasury’s “Extending Unfair Contract Term Protections to Small Businesses” consultation (“the Consultation”).

The SBDC is an independent statutory authority of the Western Australian (“WA”) Government and was established to facilitate the development and growth of small businesses in this State.

The SBDC has been providing assistance to small business owners in WA for 30 years and its vision is for “A strong and enterprising small business sector in Western Australia”.

One of the SBDC’s key strategic objectives is to advocate for a fair, conducive and productive environment for small businesses in WA. The SBDC strives to achieve this by taking a leading role in influencing the policy and regulatory environment for small business. The SBDC also develops the small business sector through the provision of education materials, workshops and tailored business and commercial tenancy advice, amongst other things. These educative and advisory services assist small businesses to better understand their rights, in order to minimise their exposure to risk and therefore to disputes.

In 2011, the *Small Business Development Corporation Act 1983 (WA)* was amended to introduce the role of the Small Business Commissioner (“SBC”) as the Chief Executive Officer of the SBDC and to establish an alternative dispute resolution (“ADR”) service to assist small businesses to resolve their business-to-business and business-to-government disputes.

In order to build up a comprehensive picture of WA’s small business sector, the SBDC has a multifaceted approach to gathering information. Statistical data about the sector is monitored from a variety of sources, including interactions with individual small businesses through the SBDC’s advisory and ADR services, as well as undertaking frequent opinion polls and other surveys of small business operators in WA. The SBDC uses this information to inform evidence based policy development and program delivery, and to advocate on behalf of the small business sector to government agencies and industry.

## **The SBDC’s submission to this consultation**

The SBDC contends that many small businesses in Australia have suffered detriment as a result of an unfair contract term being enforced against them. This submission will provide evidence and case studies to highlight the extent of this detriment not only to the small business but to its owner and their family. Further, the submission will illustrate the vulnerability of many small businesses to these practices, which is arguably on par with that of individual consumers.

The SBDC, in line with the Federal Government's policy position, will argue that legislative reform of this area is required to achieve adequate protection for small businesses as the current legislative framework and market conditions do not provide this. The SBDC supports the implementation of reform in line with Option 3 as presented by the Consultation Paper and in this submission will discuss considerations that such a reform will require. The SBDC believes that the benefits of legislative reform of this area will go beyond the small business sector and provide benefit to the wider community in general.

The SBDC's submission is backed up by 30 years of experience in assisting small businesses and therefore 30 years of exposure to the detriment suffered by small businesses subject to unfair contract terms in standard form contracts. The SBDC hopes that this submission, which is informed by the real experiences of its clients, will assist the Federal Government to justify its policy position to extend protections to small businesses.

The SBDC realizes that the biggest challenge for lawmakers conducting the review is not to show that unfair contract terms cause detriment to small businesses, but rather to implement reform that provides protection to small businesses without creating unnecessary confusion or red tape.

## **Small Business in Australia**

Unfortunately, across Government and the legislature in Australia, there is no standard, or agreed upon, definition of "small business". Some definitions are based on employee size and others on turnover, but with little consensus or consistency. The *Small Business Development Corporation Act 1983* (WA) ("the SBDC Act") defines 'small business' as a business which is owned and operated by an individual or by individuals in a partnership or by a proprietary company that has:

- A relatively small share of the market in which it competes;
- Is managed personally by the owner, owners or directors; and
- Is not a subsidiary of, or form part of, a larger business or enterprise.<sup>1</sup>

Despite the fact that there is no standard or agreed upon definition of small business in Australia, it cannot be denied that the sector has a significant impact on the economy and community overall. The SBDC believes that it is important to acknowledge the significance of the small business sector to the economy in order to ensure that the Federal and State/ Territory Governments continue to make it a priority when setting their policy agenda.

Whilst the Consultation Paper recognizes the fractured nature of the small business sector and the characteristics that differentiate them from larger businesses<sup>2</sup>, it does not document in detail the significance of the sector.

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<sup>1</sup> Section 3, *Small Business Development Corporation Act 1983*

The small business sector is the backbone of the Australian economy and a significant contributor to the general community as they employ 42%<sup>3</sup> of the nation's workforce. There are over 2 million small businesses in Australia accounting for 97.3%<sup>4</sup> of all businesses (in WA they number 208,926 or 96.7% of all businesses) and are active in all industries and sectors of the economy.

Given their overwhelming number and importance to the economy a strong case exists that small businesses are worthy of Government efforts to reduce the detriment that can result from being subject to unfair contract terms in standard form contracts.

## **Small businesses are just as vulnerable as individual consumers**

The Consultation Paper questions whether small businesses differ from consumers in relation to their interaction with standard form contracts. In the SBDC's experience, a small business may be just as vulnerable (if not more) as individual consumers to the traps of standard form contracts, especially in regards to the quantum of the detriment that can occur.

The Consultation Paper recognises that one aspect of unfairness in a contract is the fact that it transfers the majority of the risk (or all in some cases) to one party to the contract. This is usually to the weaker party that is least placed to manage the risk. The SBDC believes that in many cases a small business is in an even more vulnerable position than that of an individual consumer to manage the risk being transferred to it and often is subject to a larger amount of risk in standard form contracts than individual consumers. For example, a small business owner has personal (e.g. ability to draw a profit from the business) and commercial interests (e.g loans and other financial obligations such as payment of wages) that could be jeopardized if an unfair term is enforced against them.

The SBDC notes that the Productivity Commission in 2008<sup>5</sup> (prior to the introduction of the *Competition and Consumer Act 2010 (Cth)* "CCA 2010") recognized that small businesses are vulnerable as a consumer group and recommended that they be afforded additional protection by amending the legislation in jurisdictions where the definition of a consumer was more restrictive than that contained in the historical version of the trade practices legislation (as at 2008). As a result, small business

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<sup>2</sup> Department of Treasury 2014, *Extending Unfair Contract Term Protections to Small Businesses Consultation Paper*, Government of Australia, Available from: <http://www.treasury.gov.au/ConsultationsandReviews/Consultations/2014/Small-Business-and-Unfair-Contract-Terms> [30 July 2014]

<sup>3</sup> Australian Bureau of Statistics 2013, *ABS Cat. No. 8155.0 – Australian Industry, 2012-13*

<sup>4</sup> There were 2,079,666 businesses as at June 2013, of which 2,025,122 are classified as small businesses [1,264,298 were non employing, 563,412 employed 1 – 4 people and 197,412 employed 5-19 employees]. Source: Australian Bureau of Statistics 2013, *ABS Cat. No. 8165.0 – Counts of Australian Businesses, Including Entries and Exits June 2009 to June 2013*.

<sup>5</sup> The Productivity Commission 2008, *Review of Australia's Consumer Policy Framework Inquiry Report No 45*, Available from <http://www.pc.gov.au/projects/inquiry/consumer/docs/report> [30 July 2014]

consumers were afforded some protections in the CCA 2010; for example in relation to guarantees and warranties for goods and services (subject to meeting the eligibility criteria for these provisions).

In a recent submission to the Productivity Commission<sup>6</sup>, the SBDC highlighted the characteristics of a small business owner that makes them vulnerable to legal issues. These relate to the individual factors of the owner (e.g. age, language, cultural background) and characteristics associated with owning a small business (e.g. lack of time and money). From the SBDC's experience, many small business operators suffer detriment as a result of their lack of specialist skills and understanding of complex matters relating to running a business.

Whilst the SBDC is not saying that all small business owners share all of these characteristics, a significant proportion will have at least one of these characteristics, making them vulnerable to the legal consequences associated with unfair contract terms.

Commonly reported experiences of small business owners making them vulnerable to legal issues, include a lack of:

- time to educate themselves on common business concepts;
- time to maintain currency in knowledge;
- money to invest in improving systems, governance and models of best practice; and
- time and money to pursue complaints.

During its review of the consumer policy framework, and when considering the impact of unfair terms on small business, the Productivity Commission noted that small business operators face many of the same issues as individual consumers when dealing with larger business. This included unequal bargaining power and a lack of resources to effectively negotiate contracts.<sup>7</sup> Additionally, small business owners lack the resources and time to effectively educate themselves on these legal matters, which put them at a distinct disadvantage when it comes to contracting with a larger business.

The characteristics of small business owners have largely remained unchanged, and in the SBDC's opinion are unlikely to change. Furthermore, the pressures, such as lack of time and resources required to effectively manage their contracts (in addition to everything else a small business owner has to juggle e.g. staff, stock, rent) are unlikely to lessen for the next generation of small business owners. For this reason, the SBDC believes that legislative reform in areas causing significant detriment to the small business sector, such as unfair contract terms in standard form contracts,

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<sup>6</sup> Small Business Development Corporation, 2013 *Submission to the Productivity Commission Inquiry into Access to Justice Arrangements*, available from [http://www.pc.gov.au/data/assets/pdf\\_file/0007/129922/sub076-access-justice.pdf](http://www.pc.gov.au/data/assets/pdf_file/0007/129922/sub076-access-justice.pdf) [30 July 2014]

<sup>7</sup> Ibid 6, page 318

is required to remedy this disadvantage. Expecting the problem to resolve itself without legislative reform is unrealistic and impractical.

## **Standard form contracts and small business**

The SBDC agrees that standard form contracts are beneficial for small businesses offering such agreements to their clients, as it saves time and money. However, as recognized by this consultation, the detriment that arises when an unfair contract term is included in a standard form contract can be significant for a small business.

To help inform this submission, small business clients of the SBDC were invited to complete a short online survey<sup>8</sup> to ascertain their experiences with unfair terms in standard form contracts. It should be noted that this survey was not as comprehensive as the survey developed by the Federal Government and the sample size was not large enough to allow for significance testing of results. Nonetheless, the results are useful as it provides an insight into the types of issues arising for WA small businesses subject to unfair contract terms.

When questioned about their use of standard form contracts, 80.6%<sup>9</sup> indicated that their small business was party to a standard form contract, with almost half offering them to their clients. Of those that were party to a standard form contract, 42.1% indicated that most of their contracts were standard form while 28% indicated that a few were standard form. Approximately one-fifth of respondents (19.3%) indicated that none of their contracts were standard form. In a previous survey conducted by the SBDC in 2012<sup>10</sup>, small businesses were asked whether they had used a legal professional to draft their contracts with over half (55%) indicating that they drafted the contract themselves.

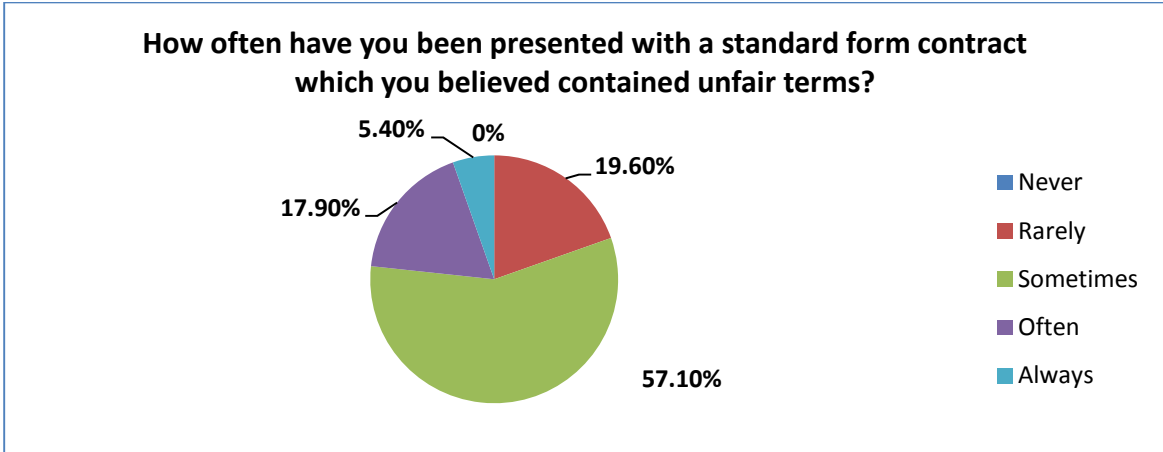
In the SBDC's unfair contract term survey, respondents were asked "how often have you been presented with a standard form contract which you believed contained unfair terms". Responses to this question indicate that all respondents had been presented with an unfair contract term at some point, as shown in the graph below:

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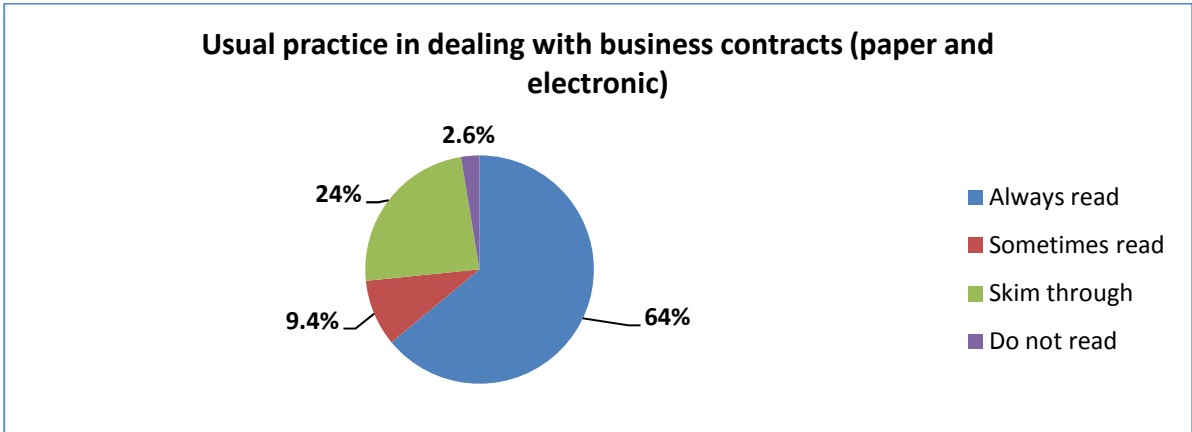
<sup>8</sup> The "Unfair Contract Terms" online survey consisted of 20 questions and was open to the business owner or manager with responsibility for the business contracts. Based on this eligibility there were 89 valid responses to the survey. The *n* for each question differs as respondents were not required to answer every question.

<sup>9</sup> Please note that the total respondents to this question were less than the total that completed the survey. Therefore, this reflects the answers of a subset of the respondents.

<sup>10</sup> The SBDC conducted a short survey of 63 small businesses in WA in 2012, titled "Business Contracts Survey".

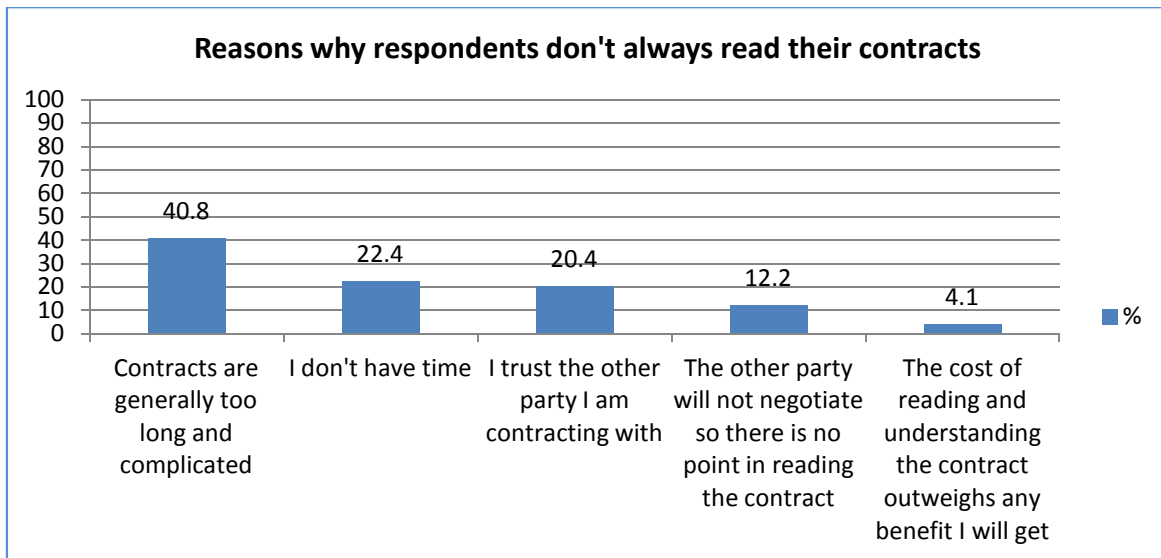


The majority of respondents (73.4%) also claimed that they either always (64%) or sometimes (9.4%) read through the contents of their contracts. This is in contrast to the results of previous SBDC surveys<sup>11</sup>, however this does not necessarily mean that small businesses are improving their practices around contracts. The current survey reveals that a quarter (24%) of small business respondents still typically only skim through the contents of their business contracts. These results are displayed graphically below:



Survey respondents who indicated that they did not always read their contracts (e.g. those that answered ‘sometimes’, ‘skim through’ or ‘do not read’) were then asked what prevented them from always reading their contracts. As shown graphically below, 40.8% believed that the contracts were too long and complicated, with 22.4% not having the time and 20.4% reporting that they do not read the contract because they trust the other party.

<sup>11</sup> The results of the SBDC’s Business Contracts Survey indicated that less than half (48%) of respondents always read through all of their contracts.



It would appear that the small business respondents who completed the SBDC's unfair contract terms survey are generally confident in their ability to understand the terms of the contracts, when they do actually read them. The majority of respondents (72.9%) agreed or strongly agreed with the statement "of the contracts I have read, in general I was confident that I understood the meaning of the key terms and their implications for my business".

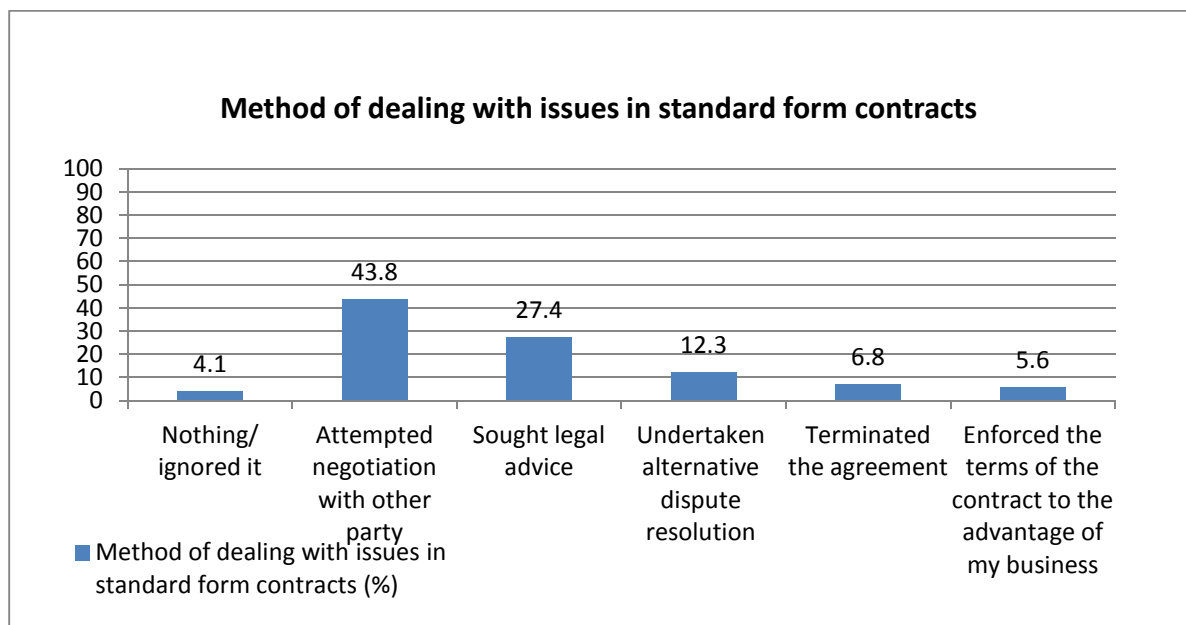
Based on these results, it would appear that small businesses in general are reading and understanding contracts, however this does not seem to necessarily help them avoid problems with unfair terms in standard form contracts. This may be due to the belief that they are powerless to negotiate the terms of the contract and therefore enter an agreement that was less than favourable to their business. As shown in the table above, 12.2% of that subset indicated that they do not read the contract because they believed that the other party would not negotiate the terms anyway. It would appear that this belief was not unfounded as of those businesses that had experienced a standard form contract, 40% disagreed or strongly disagreed with the statement "the other party [was] willing to negotiate the contract terms with me". Furthermore, for those respondents who had been offered a standard form contract, 68.9% indicated that it had been offered on a "take it or leave it" basis.

These results also reveal that some small business owners will still try to negotiate the terms of a contract despite the reluctance of the other party. When asked to reflect on an actual experience with an unfair contract term, 40% of respondents (n=45) disagreed or strongly disagreed with the statement "In general, I have the power to negotiate to change the terms I believe are unfair". Despite this, the majority (82.2%) of these respondents had tried to negotiate the terms of a standard form contract.

The survey then asked respondents what they did when presented with a contract that contained terms that may be unfair to their small business. Around half (48%) indicated that they had refused to enter the contract.



Those respondents who had been party to a standard form contract were then asked whether issues had arisen and what they had done about it. A small minority (3.9%) indicated that issues had never arisen in their standard form contract. For those that had encountered an issue, the most common method of dealing with it was to attempt negotiation with the other party, followed by seeking legal advice and undertaking alternative dispute resolution, as depicted in the graph below.



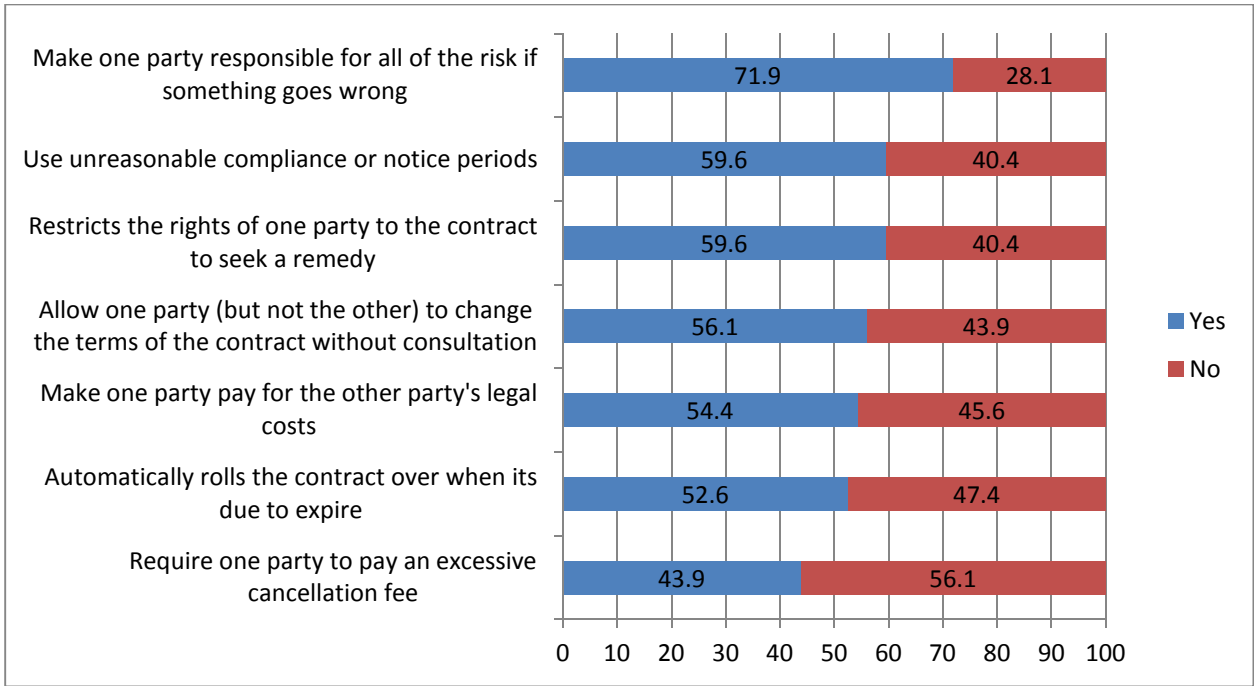
## Unfair contract terms for small business

As outlined in the Consultation Paper, the Australian Consumer Law (“ACL”) currently provides protection against unfair terms in standard form individual consumer contracts for the supply of goods and services or the sale or grant of an interest in land.<sup>12</sup> It also defines “unfair” as it relates to terms of standard form contracts to which individual consumers are party to<sup>13</sup>. In order to elicit examples of unfair contract terms from our small business respondents, the SBDC compiled a list of “unfair terms” that met this definition.<sup>14</sup> Survey respondents were presented with this list and asked whether they had entered into a contract that contained such a term, the results of which are displayed below:

<sup>12</sup> Section 23 of Schedule 2 of the Competition and Consumer Act 2010 (Cth), referred to as the ACL

<sup>13</sup> Ibid, Section 24

<sup>14</sup> That is terms that cause a significant imbalance in the parties’ rights and obligations under the contract; would cause detriment (financial or otherwise) to the party if it were to be relied on; and was not reasonably necessary to protect the legitimate interests of the party who would be advantaged by the term.



Small business respondents were then asked to indicate which term they believed to be most unfair from the list provided. The terms that small business respondents believe were most unfair were, ranked from most to least mentioned:

1. Allows one party (but not the other) to change the contract without consulting the other party;
2. Use unreasonable compliance or notice periods;
3. Make one party responsible for all of the risk if something goes wrong;
4. Restricts the rights of one party to the contract to seek a remedy if something goes wrong;
5. Make one party pay for the other party’s legal costs;
6. Automatically rolls the contract over when its due to expire; and
7. Require one party to pay an excessive cancellation fee.

Despite these survey results the experienced team of Business Advisers at the SBDC believe – based on their client interactions – that small businesses in WA encounter the most problems with automatic rollover clauses. They generally have ongoing financial impacts, often for sub-standard services (explained in more detail later).

***Terms that have the effect of deceiving or tricking the party***

The SBDC has collected evidence of specific terms that in effect could be used to deceive the weaker party and therefore have the potential to be unfair. Example clauses with this effect are outlined below:

“The Licensor and Licensee agree that this licence is personal and any rights rest in contract only and do not create a tenancy or leasehold interest in the

License Area or confer any rights under the tenancy legislation” [Casual Leasing Agreement]

“Unless agreed to the contrary in writing by [Company name], [the] Customer is to pay for any and all charges, usage costs, maintenance charges and any other cost associated with [a list of charges]” [Equipment Hire Agreement].” This is despite the Company’s website and advertising stating: “[Company name] provide ATM’s for free.”

“The Licensor may, within its absolute discretion and at any time before the Start Date or during the Licence Period, relocate the Licensee to another site within the Centre if it considers it necessary. The Licensee must immediately comply with the Licensor’s directions in this regard.” [Casual Leasing Agreement]

### ***Restrictive terms***

Terms that restrict the rights of one party to the contract without being reasonably necessary to protect the other party’s legitimate interest are, in the SBDC’s opinion, unfair and have the potential to cause significant detriment. Examples of this type of term were prevalent in the contracts being presented to the SBDC’s clients and have resulted in financial cost and a loss of opportunity to expand a business among other things.

By way of examples, the SBDC has heard from many small business operators who have signed standard form contracts for advertising services. This included advertisements on closed circuit television screens in a medical centres, and gymnasiums. Feedback from SBDC clients suggests that the services provided by these contracts is typically substandard and does not represent value for money. Further to this, it appears that the companies offering these services try to prevent small business customers from cancelling the contract. This is best evidenced by the term below, which was found in such a contract:

*“This contract is not subject to cancellation by the Advertiser”* [contract for advertising services between a small business and advertising company]

Other standard form contracts seek to restrict the ability of the smaller party to expand their business by preventing them from on-selling products or including clauses that prevents them from offering a wider product range, as shown by the comments below from respondents to the SBDC’s unfair contract terms survey:

*“Unreasonable exclusion to competing products for 3 years after expiry of term.”* [survey respondent, unfair contract terms, 2014]

*“Restriction for on-selling to other organizations.”* [survey respondent, unfair contract terms, 2014]

Restrictive terms are also found in commercial tenancy leases:

*“It is unfair because it restricts our ability to continue as we have done for the past 11 years through significant reduction in area leased, excessive restrictions on how we operate eg. on each occasion having to get written permission from the lessor to allow any ‘for profit’ entity or person to assess the premises. This is simply unworkable”* [survey respondent, unfair contract terms, 2014]

### ***Automatic Rollover Clauses***

Many companies that provide substandard products or services often also use automatic rollover clauses in their standard form agreements. In most cases, the contract will automatically rollover for another period unless the small business owner follows the often quite onerous notice requirements in the contract. The period in which notice must be served is usually excessive, for example:

“On the expiry of the Initial Period, this Agreement automatically extends for a further term of 1 year (“Further Period”) unless either party gives notice to the other that it wishes to terminate three months prior to the expiration of that further term.” [Equipment Hire Agreement]

As a further example, the clause below requires the other party to serve notice by certified mail. This is not a common form of communication for modern businesses, who may assume that notice can be communicated by more practical methods such as email, fax or standard post:

“...If the Advertiser does not wish for their advertisement to appear after the expiry of the Initial Advertising Period the Advertiser must serve notice in writing by **Certified Mail** to that effect to the Company no later than 12 months after the date on this agreement, failing which the Agreement will become a 12 month rolling contract....” [contract for advertising services]

In this situation, the larger business preys on the smaller business operator’s vulnerability because quite often they miss the cut off date to give notice due to the fact that they are time poor and have more pressing issues to concentrate on. The detriment suffered by the small business in these cases is that they often have to pay a substantial amount of money for a substandard service or product

This type of term is frequently found in contracts for online advertising services, as shown in the case study below:

### *CASE STUDY – ADVERTISING SERVICES*

Multiple small businesses have contacted the SBDC complaining about being caught out by an automatic rollover clause in their [Company Name] advertising contract. The small businesses complain that they agree to this clause, often verbally over the telephone, but fail to take the necessary steps to ensure that they terminate the contract within the specified notice period. Many small businesses who have been caught out by this clause acknowledge the legality of the clause; however complain about its unfairness and how much it costs them to continue with the contract for another year.

Automatic rollover clauses are also found in contracts for screen advertising:

### *CASE STUDY – ADVERTISING SERVICES: SCREEN ADVERTISING*

The SBDC has received a number of complaints from small businesses who have contracted with a private company offering advertising services on closed circuit television screens in medical centres. The complaints centre on the automatic renewal clauses contained in these contracts and a lack of consistency of services. Clients have also complained that sales staff pressured them into the sale and made false representations that the client could cancel the contract or that the contract term would expire after 12 months, when in fact hidden in the terms and conditions was the automatic rollover clause.

In one case, a client was advised by the medical centre that the screen was faulty and that the advertising company refused to fix it therefore it was mostly turned off. The medical centre also complained that they were unable to cancel their contract with the advertising company. The client was faced with either a large cancellation fee that did not seem to reflect the price of the contract, or continuing with the contract.

The contract contained clauses such as “this contract is not subject to cancellation by the Advertiser”; “this is an automatically renewable advertising services agreement, and not for the sale of goods”.

Standard form contracts for the hire/ lease or placement of goods in a small business also frequently contain automatic rollover clauses, as shown by the case studies below:

### CASE STUDY – EQUIPMENT HIRE

A small business owner entered a contract to hire a piece of office equipment for a 5 year period. The contract had a clause that required the lessee to inform the lessor of their intention to renew the contract 90 days before it was due to expire. The small business owner did not provide notice within this period and was held to the contract renewal period of a further 6 months. This prevented the small business from purchasing a new piece of equipment that better served his business need.

### CASE STUDY – ATM PLACEMENT

A small business entered into an agreement with a private company to place an ATM in her shop for a period of 5 years. A week prior to the contract expiring the small business owner gave written notice that she did not intend to renew the contract. The private company declined the written notice citing a clause in the contract that required 180 business days notice of this intention prior to the end of the contract. The private company informed the small business that the contract would rollover and be extended for a further 5 years. The client was unaware that the contract they signed had this clause in it and felt that it was unfair.

Automatic rollover clauses were also the subject of complaints from numerous small business respondents to the SBDC's unfair contract terms survey. Small businesses often find such terms confusing and complain about the unfairness of paying for services that are substandard and for 'hidden costs':

*"Confusion over when an advertising contract was signed and implementation of advertising and automatically rolling into another two year rolling contract after the first two year's advertising was paid in the first year.... always paying for two years in one and then forced to pay 3rd and 4th year in the second year"* [survey respondent, unfair contract terms, 2014]

*"two year rolling advertising contracts that are paid in the first 12 months and then automatically rolled into 3rd and 4th year payments during the second year are unfair and a pyramid scheme"* [survey respondent, unfair contract terms, 2014]

*"The extent of 'hidden' costs caused by some standard contracts over time, especially in periods when no service is delivered, can be great. If you have a couple of these (e.g. communications and service assistance) then you can use significant amounts of money if you are not vigilant. Getting out of these contracts can be more time consuming than the cost of paying them out. Not a fan."* [survey respondent, unfair contract terms, 2014]

## ***Unreasonable Payment Terms***

Contracts that include a long payment term, which delays when a small business receives payment for a good or service rendered, can cause significant but avoidable detriment to small businesses. These terms are the subject of many complaints received by the SBDC and whilst a lot of complaints stem from small businesses in the building and construction industry, these types of terms are common across industries. Examples include:

“Payment shall be 100% forty five (45) days from end of month and receipt by Purchaser of correct and proper invoice and further supporting documentation following delivery of Goods to the delivery point stated in the Order” [Purchase Order Terms and Conditions]

“[Company name] will accrue all invoices rendered by the Supplier for the period between the 5<sup>th</sup> day of each month and 4<sup>th</sup> day of the following month ) Accumulation Period) and [Company Name] will pay all invoices rendered by the Supplier 90 days from the last day of the Accumulation period.” [Supply Agreement]

The effect of the example clause above is a potential delay in payment to the supplier of up to 120 days. A delay in the payment of outstanding monies owed to a small business can be catastrophic. Good cash flow management is essential for a small business to stay afloat, and prompt payment by customers is necessary to operate efficiently and to cover business expenses.

While often a small business will be expected to wait for an unreasonable period before receiving payment, it will be required to make a much quicker payment to larger companies, as shown in the comment by a survey respondent:

*“Big businesses (like Telstra) wanting you to pay them for services within 7 or 14 days, but if they owe you, they will wait 60 or 90 days [to pay you].”* [survey respondent, unfair contract terms, 2014]

## ***Excessive Cancellation Fees***

Small businesses are also often subject to hefty cancellation fees if they choose to cancel a contract before its expiration date. Whilst the SBDC accepts that a cancellation fee may be required to cover the reasonable costs incurred by the other party as a result of early termination, it believes that this should be limited to the amount of actual loss. It is unfair to charge a small business a fee that exceeds the actual loss of the other company, particularly if that company is able to mitigate its losses.

In the clause below, the customer is agreeing to pay an unspecified and unlimited amount in cancellation fees. Further, this clause does not specify that the termination

is initiated by the customer, so it could be argued that the cancellation fee is payable by the customer even if the termination is initiated by the company offering the contract:

“Clause 18(3): Customer acknowledges that termination of this Agreement before installation for any reason or refusal to accept delivery and installation of the equipment for any reason will result in Customer being immediately liable to pay the Cancellation Amount which is considered fair and reasonable compensation for damage suffered by [Company Name].” This is followed up by Clause 22(a) “...A Cancellation Amount of no less than, but not restricted to \$3,300 including GST will be charged...” [Equipment Hire Agreement]

### *Unfair Terms in Retail Tenancy Leases*

Through its specialist commercial tenancy advisory service, the SBDC receives many complaints from small business tenants regarding the perceived fairness of their retail lease. Complaints relate to the landlord’s ability to move the small business to a different tenancy or to cancel the lease if they so wish. In some cases the landlord will use a licence arrangement instead of a standard lease document in order to try and avoid being subject to the protections offered to tenants by the *Commercial Tenancy (Retail Shops) Agreements Act 1985 (WA)*. This is shown in the example below:

#### *CASE STUDY - COMMERCIAL LEASES*

A small business tenant signed a short term lease (which was presented in the form of a licence agreement) and at the request of the managing agent for the landlord, paid approximately \$14,000 for equipment required for the shop fit out. Prior to the client taking possession of the premises the managing agent terminated the agreement with an explanation that the premises was to be leased to another client who was able to sign a longer term agreement.

The managing agent cited a clause in the agreement that stated “... *the Licensor [the landlord] may at any time for its sole convenience terminate this licence by written notice to the Licensee [the tenant]. If the Licensor terminates this licence under this clause 4.3 the Licensee... will not be entitled to make any claim against the Licensor for any loss, damage, cost or expense the Licensee suffers in relation to the termination.*” (emphasis added). In this case the small business tenant was able to claim back part of the money paid to the landlord under the agreement but was not able to make a claim for the expense incurred purchasing the equipment to fit out the premises.



The SBDC has also heard about the introduction of clauses in retail tenancy leases as a result of the 2011 amendments to the *Commercial Tenancy (Retail Shops) Agreements Act 1985* (WA). Section 13C of this Act requires that the landlord provides notice to the tenant of an option or further option to renew the lease. The purpose of this is to ensure that tenants who have an option to renew a lease do not lose this right because they inadvertently missed the notice date. In response to this amendment, it would appear that some landlords are inserting provisions into retail leases that place the onus back on tenants by requiring them to inform the landlord of their intention to renew the lease prior to the period specified by section 13C. According to the SBDC's Business Advisers, this can be particularly onerous for tenants with long leases.

Similarly, the SBDC is aware of situations where landlords and management agents are charging excessive amounts for the assignment of leases. This is evidenced from the comment below from a survey respondent:

*"The real estate agent required an excessive fee for the assignment of an existing lease [approximately \$5,000], and wanted to charge us management fees although prohibited under the Commercial Tenancy Act."* [survey respondent, unfair contract terms, 2014]

### ***Terms requiring the party to accept excessive risk***

The SBDC is aware of standard form contracts that contain terms that require the other party to take on excessive risks or provide unreasonable warranties. The clause below requires the small business to warrant that specific equipment will not be placed in the vicinity of their shop. In practice, the small business operator is not in a position to do this as they are unlikely to have any control over the immediate vicinity of their premises:

*"The Customer warrants that the Equipment is and will be for the term of this Agreement the only cash-dispensing equipment on and in the immediate vicinity of the Customer's Premises."* [Equipment Hire Agreement]

Small businesses are also being stung by standard form contracts that require them to provide extended warranties for goods and services they sell. The effect of some of the clauses used in standard form contracts is that a warranty is provided which may exceed that required by the ACL. This is demonstrated below:

*"Supplier shall (at the option of the Purchaser) either replace or repair and make good any Goods or parts of Goods supplied by it found to be defective in any way unsuitable for the purpose interested for a period of twenty four (24) months from the date of delivery of Goods. If Supplier repairs or replaces Goods during the warranty period then a new warranty shall apply to those Goods for a period of twenty four (24) months from the date such repairs or replacements were completed."* [Purchase Order Terms and Conditions]

The SBDC was interested in exploring terms that make one party accept most or all of the risk under the contract, regardless of their ability to manage that risk. Through our survey, we explored small business owners' understanding and experience of contracts that pass on the risk by assessing their agreement (or otherwise) with a number of statements. It would appear that most small business respondents do take into consideration the risk when signing standard form contracts, and also understand that they are taking on extra risk that would usually be borne by the other party. Results suggest that small businesses owners are taking on this additional risk despite the fact that they are not in a position to manage the risk adequately (financially or otherwise). The results of these statements are displayed in the table below:

**Table: How small businesses consider and manage risk in contracts**

	Strongly disagree (%)	Disagree (%)	Neither (%)	Agree (%)	Strongly Agree (%)
I do not think about risk to my business when signing standard form contracts	42.2	40.0	8.9	6.7	2.2
I understand that by signing a standard form contract, I am taking on extra risks that would usually be borne by the other party	2.2	22.2	22.2	37.8	15.6
My business is in a position to manage the risk adequately	17.8	24.4	26.7	26.7	4.5

\*n=45

### ***Terms allowing one party to unilaterally change or terminate the agreement***

Many of the goods and services (e.g. telephone, insurance, advertising) provided to small businesses under standard form contracts are often vital to their operation. As a result, a small business that relies on these services could suffer serious detriment if the service ceased to be provided due to the unilateral decision of the supplier to terminate the contract. Examples of some of these clauses include:

“The Company reserves the right for any reason whatsoever to withhold, withdraw or refuse any advertisement.” [Contract for Advertising Services]

“Purchaser may at its option cancel the Order or any part thereof at any time.” [Purchase Order Terms and Conditions]

“[Company name] may immediately terminate the Agreement for any reason and at any time.” [Equipment Hire Agreement]

“[Company name] can remove the Equipment from the Customer’s Premises at [Company name’s] cost and immediately terminate the Agreement for any reason and at any time” [Equipment Hire Agreement]

In some cases, the termination clauses are particularly harsh for small business customers if they limit the redress for loss caused by the early termination of the contract:

“In addition to any other rights the Licensor has under this licence, the Licensor may at any time for its sole convenience terminate this licence by written notice to the Licensee. If the Licensee terminates this license under clause 4.3 the Licensee... (c) will not be entitled to make any claim against the Licensor for any loss, damage, cost or expense that the Licensee suffers in relation to the termination” [Casual Leasing Agreement]

Terms that allow one party to unilaterally vary the service provided under the contract can also be detrimental to small businesses. As shown below, some terms allow the party offering the contract to change essential terms of the contract which impact on the product being delivered:

“The Company reserves the right to change the shape, size, title and locale of the advertisement.” [Contract for Advertising Services]

The SBDC has even come across terms in a standard form contract offered to small businesses that allow the other party to unilaterally change the most essential term of the agreement – that is the parties to the contract. This is shown below:

“The benefit of this Agreement is capable of transfer or other disposal by the Company (but not the Advertiser) to any third party in whole or part” [Contract for Advertising Services]

Small business respondents of the SBDC’s unfair contract terms survey indicated that they felt terms that allowed the other party to change the price of the goods or services offered, or allowed them to charge unspecified amounts, were unfair:

*“All liability fell on my business and they could change the terms of contract without notifying me”* [survey respondent, unfair contract terms, 2014]

*“Unspecified outgoings [is an example of an unfair term]”* [survey respondent, unfair contract terms, 2014]

*“[The term] allowed [the] supplier to automatically increase costs regardless of surrounding economic circumstances and practices”* [survey respondent, unfair contract terms, 2014]

In summary, the case studies and survey results presented above suggest that remedial and operative terms are equally concerning for small business and both have the potential to cause significant detriment.

## Unfair processes

As alluded to in the Consultation Paper, sometimes it's not the actual term that is unfair but the way in which the contract is negotiated or the processes involved in executing the contract.

The SBDC's unfair contract terms survey explored this issue by asking respondents to indicate which process, from a prepared list, had caused them difficulties. Ranked from most to least mentioned, the following processes are identified as being problematic for small businesses:

1. Negotiating the terms;
2. Dealing with a dispute when it arises;
3. Getting the other party's consent to make changes to the contract;
4. Terminating the contract early;
5. Dealing with a default under the contract;
6. Winding up the contract when it comes to an end; and
7. Executing the contract.

To explore the extent of the unfairness in the process of standard form contracts the SBDC has gathered case studies of our clients' experiences, which follows.

### *"Take it or leave it"*

The Consultation Paper recognised that standard form contracts are offered on a "take it or leave it basis" as often the receiving party needs the service/ products and has little power to negotiate better terms.

This is a reality for many small businesses and was reflected in the results of the SBDC's unfair contract terms survey, as shown by the comments below:

*"Generally they are take it or leave it and you as a micro business have no choices and have to bow to the fact that the service is essential even if you don't like the terms."* [survey respondent, unfair contract terms, 2014]

*"Banks are the worst of all, there [sic] contracts are all one sided and have take it or leave it attitude, along with their legal people, some banks will bankrupt you to avoid you challenging them, I am going through major issues on this at present, they have caused me huge financial losses."* [survey respondent, unfair contract terms, 2014]

### *CASE STUDY – SUPPLY AGREEMENT*

A small petrol station had a contract with a large fuel distributor to badge their store and supply it with fuel. Under their supply agreement, the small petrol station owner was also able to source fuel from other suppliers and enter agreements with other parties to transport the fuel to their station from the source. This allowed them to reduce their freight costs by \$70,000 per year. When the contract expired and the petrol station owner tried to negotiate a new contract, the large fuel distributor offered them a contract which excluded them from making their own arrangements for the transport of the fuel or purchasing from other distributors. The contract was offered on a “take it or leave it” basis without the ability to negotiate. If the petrol station owner did not enter the agreement with the large fuel distributor, they would have to re-badge their store to another supplier and lose out on the benefits received under the previous contract (such as brand goodwill).

### *Presenting complex terms and conditions verbally or externally to a written contract*

Alarming, the SBDC has become aware of situations in which small businesses are presented with a standard form contract, which includes additional terms and conditions that are only available externally to the contract (such as online):

### *CASE STUDY – TERMS AND CONDITIONS DISPLAYED EXTERNAL TO THE CONTRACT*

The SBDC is aware of multiple contracts (across product type and industry) where the terms and conditions are contained in a separate document which is usually only accessible in an online format. In some cases, the links provided to these terms and conditions are broken and therefore a business is required to accept the terms and conditions without actually seeing them

In the taxi industry, drivers are presented with updated terms and conditions on the screen in their vehicle and cannot proceed unless they accept these terms and conditions:

### *CASE STUDY – NOTIFICATION OF CHANGING TERMS*

A small business taxi operator contacted the SBDC complaining about the operating agreements of a Taxi Dispatch Company. These agreements give drivers access to the dispatch system and are vital for business. However, notifications of variations to the agreement are only presented to drivers on the computer screen located in the taxi. As such a driver is required to accept the variation as soon as the notification pops up on their screen and cannot access the dispatch system until they have done so. This process adopted by the Taxi Dispatch Company is inherently unfair and could induce drivers to accept unfair contract terms or lose access to jobs.

Small businesses are also being presented with terms verbally and must agree to accept them on the spot. This process is inherently unfair as the client is expected to listen to, understand and give informed consent to complex terms and conditions without the benefit of having time to read and digest them, or seek expert advice if needed, as shown below:

### *CASE STUDY – VERBAL PRESENTATION OF COMPLEX TERMS*

A small business owner contacted the SBDC for help over a dispute with a Company regarding an advertising contract. According to the client, they were told by the Company representative that she could cancel the contract within 3 months if she was unhappy with the service (similar to a cooling off period). When she went to cancel the contract within this period, the Company refused citing a recorded conversation between her and the company representative in which she verbally accepted the term. The client complained to the SBDC that the Company would only give her access to one minute of the phone recording but refused to play her the rest of the recording in which she is adamant that the sales representative led her to believe that she could cancel the contract within the 3 month period. As a result, the client was faced with paying a fee to cancel the contract prior to its expiry.

### ***Bully tactics to induce a party to enter a contract***

The SBDC has heard anecdotally of supervisors of well known construction companies pressuring subcontractors to sign agreements and using statements such

as “nobody reads them anyway”, “they are just a formality”, “you can’t start work until you sign it”.<sup>15</sup>

*“The use of the terms in [agreements between builders and subcontractors] are allowing the builder to use extortion, bullying and intimidation.”* [survey respondent, unfair contract terms, 2014]

In some cases, the party offering the contract preys on the vulnerability of the small business operator who may not know their legal rights or be able to afford legal advice:

*“I was offered a termination agreement where I was threatened with legal action if I did not agree to it. [The other party] was very aware of the fact that I did not have the money to start going to court and, I was forced to sign away my Copyright ownership to work that I had produced and spent a lot of time on, walking away empty handed. I agreed to do it because I could not get any legal advice without spending any money.”* [survey respondent, unfair contract terms, 2014]

*“Many companies who develop standard contracts are sham organisations who bully people who deal with them, and threaten the small business if they disagree with the terms and conditions. However each party can make changes, but most Small Business owners have no idea how to do this as they have NEVER studied any Law subjects at university level.”* [survey respondent, unfair contract terms, 2014]

*“An energy contract did not mention solar power however when we went to install it our provider refused to provide us with the information we needed to go ahead with the installation without signing a new contract on less favourable terms. There is nothing protecting us (the ombudsman does not deal with this) so the only action we have is legal action which will cost us more than waiting out the contract for 6 months.”* [survey respondent, unfair contract terms, 2014]

## Where are the unfair terms?

In the SBDC’s opinion, standard form contracts with unfair terms are used in every industry in which small businesses operate and for all types of goods and services utilized by most types of small business.

Small business respondents of the SBDC’s unfair contract terms survey were asked what types of agreements contained unfair contract terms. According to the respondents, the following agreements contain unfair contract terms (ranked in order of most mentioned):

1. Telephone and internet services;
2. Banking and financial services;
3. Leases for commercial premises;

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<sup>15</sup> As cited in personal communication from a small business client, received 21 July 2014

4. Tender documents (for government and private tenders);
5. Advertising and promotion;
6. Utilities (electricity and water); and
7. Equipment hiring/ leasing.

Other types of contracts mentioned by respondents include employment contracts, construction contracts between builders and sub-contractors, supply contracts for goods and materials for exclusivity to region and food supply.

## **The extent of detriment suffered by small businesses due to unfair contract terms in standard form contracts**

In preparing this submission, the SBDC heard from a number of small business owners regarding the type and extent of detriment they experienced as a result of having an unfair contract term enforced against them. The detriment is not limited to financial loss as these situations may also impact on personal health and relationships, and can destroy business relationships. Sadly, it appears that some small business owners have been driven to despair as a result of an unfair term in their standard form contract, as highlighted by the comment below:

*“The result [of unfair contract terms in standard form construction contracts] has caused the cost of housing to increase, [as well as] labour and destroying businesses and people’s lives. Some actions done in bad faith by these principal contractors or builders have caused people to take their lives.”* [survey respondent, unfair contract terms, 2014]

Survey respondents were asked to think about one example of a standard form contract that contained an unfair term and the detriment caused by this term. Financial loss was the most commonly mentioned detriment (30.6% of all responses), followed by loss of business opportunity (15.9% of responses); the creation of compliance obligations that required unreasonable time and effort to address (15.9% of responses) and reputational damage (12.5% of responses).

## **Options for reform**

### **Reform is necessary**

The SBDC strongly supports legislative reform to extend the protection against unfair contract terms in standard form contracts to cover small businesses. As discussed earlier in this submission, small businesses may be just as vulnerable to unfair contract term as individual consumers. In fact, it is likely that small businesses could suffer a greater detriment as a result of an unfair contract terms than an individual consumer due to the overall value and length of the of the contract. As highlighted in the above case studies, a small business can be destroyed as a result of an unfair contract term being enforced against them. This can lead to financial and personal ruin for the small business owner and their family.



The SBDC has considered all options presented by the Consultation Paper and strongly supports Option 3 (legislative amendment to extend unfair contract term protections to small business). In this context, the SBDC does not support Options 1, 2 or 4 as the current regulatory framework and market forces do not provide adequate protection to small businesses against unfair contract terms, nor do they provide adequate remedies if issues arise.

### **The SBDC does not support Option 1, 2 or 4**

The SBDC does not support Option 1 of maintaining the status quo. Whilst the SBDC acknowledges that there are some legislative mechanisms that, by default, protect small businesses from unfair contract terms, we believe that they are insufficient. They do not apply across the sector; therefore they do not provide a blanket protection for all small businesses. Furthermore, where these mechanisms do apply to small businesses, the redress they provide is not always sufficient.

The SBDC acknowledges that changes arising from the introduction of prohibitions against unfair contract terms for consumers<sup>16</sup> may have a flow on benefit to the small business sector if companies remove terms from the standard form contracts that they offer across their customer base (including individuals and small business). However, it is also an assumption that businesses may not distinguish between individuals and small businesses when offering standard form contracts and that small businesses and individuals are utilizing the same goods and services offered through standard form contracts. It is not enough to rely on this assumption to provide protection for small businesses. As shown by the case studies presented above, the standard form contracts offered to small businesses can be different to those presented to individual consumers. For example, an individual consumer is unlikely to sign a principal-subcontractor building agreement, require advertising in a gym or medical centre or require search engine optimization services.

Furthermore, under the current framework<sup>17</sup>, small businesses have no recourse when faced with an unfair contract term. Assuming there are no mitigating factors that may void the contract (e.g. capacity), the other party has a legal right to enforce the term, no matter how unfair it may be. The small business owner who has signed a standard form contract has voluntarily agreed to the terms of that contract and therefore is legally bound by it. Whether or not the small business owner has read or understood the contract is of no relevance to the enforceability of the contract.

Other provisions in the CCA 2010 protect small businesses from unfair practices and conduct in a consumer context. For example small businesses are protected from misleading and deceptive conduct under Part 2-1 and unconscionable conduct under Part 2-2 of the ACL. However neither of these prohibitions prevent the inclusion of unfair terms in standard form contracts to which a small business is party. As pointed

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<sup>16</sup> Ibid 13

<sup>17</sup> Ibid 15

out in the Consultation Paper “unfair” does not equate to “unconscionable” and this point has been confirmed by the Court in *Attorney-General v World Best Holdings Ltd.*<sup>18</sup>

The problems associated with seeking redress to legal issues arising under a contract are felt across the small business sector. One such industry that illustrates these problems is the building and construction industry.

According to an SBDC client operating in the building and construction industry who has tried all avenues to seek redress to the multiple contractual disputes he’s experienced; the three options available to him as a subcontractor in a contractual dispute with another company are far from ideal. The first option presented, adjudication under the *Construction Contracts Act 2004 (WA)*, was described as a “*very expensive headache*”. Under this Act the claimant has 28 days from the date that the payment was due and must provide proof that the claim has not been paid in full, or at all. A claimant who can meet this requirement has access to the rapid adjudication process available under the Act.

Whilst this sounds good in theory, in reality it may not be as easy to access for small businesses as it would seem. Due to common business practice and in the interests of preserving business relationships (e.g. trying to negotiate for the payment of overdue monies or acting in good faith to extend payment deadlines), it is hard for a small business to make its claim within 28 days of the payment becoming overdue. This process also does not prevent the inclusion of unfair terms into subcontractor contracts, nor does it lessen the detriment of a business subject to an extended payment period term.

The second option is via alternative dispute resolution (such as the service provided by the SBDC). Through this avenue a party could try and negotiate a better outcome as a result of having an unfair contract term enforced against them. For most parties using ADR services the outcomes are beneficial. However, for businesses in dispute with a recalcitrant party, this option can prove troublesome if it is used as a delay tactic to avoid an outcome.

Thirdly, the small business can take court action if the other party fails to make a payment under the contract. Again, this process does not prevent the inclusion of unfair payment terms in a subcontractor’s standard form contract nor does it lessen the detriment arising from such a term. Court action is typically the last resort for a small business given the significant impost this has on time and monetary resources, not to mention the stress involved or the fact that even with a court order the business is not guaranteed to get their outstanding money.

In the SBDC’s opinion, what is needed in this situation is legislative intervention to prevent the problem occurring in the first place. Having a prohibition in the CCA 2010

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<sup>18</sup> (2005) 63 NSWLR 557

(Cth) will act as a disincentive to the inclusion of unfair terms in standard form contracts, which in turn will lessen the detriment faced by small businesses that are party to standard form contracts. Furthermore, it will likely prevent disputes that have the potential to ruin business relationships relied upon by small businesses for the success of their operations.

Similarly, the SBDC does not support Option 2, which is a light touch regulatory option. The SBDC notes that the Productivity Commission<sup>19</sup>, when exploring consumer law issues concluded that light handed approaches (specifically better disclosure of terms likely to cause a problem) were unlikely to represent a satisfactory solution as they assumed the problems arose from consumer ignorance when this is not always the cause of the problems. According to the report<sup>20</sup> for most low-cost standard form contracts, consumers trust a supplier and trust that nothing will go wrong and pointing out problematic terms to them would be unlikely to have any impact. Arguably, the same would apply to small businesses faced with a standard form contract.

Additionally, the proposal under Option 2 does not address the fact that small businesses do not have the power to negotiate terms, nor the time to thoroughly read and understand the contract. Furthermore, this option requires co-operation and cohesion amongst industry bodies which may not be a practical reality. It also fails to address the issue that the small business sector is highly fragmented and cuts across all industries. Therefore, an industry led approach will not cover all small businesses.

The SBDC does not support Option 4, which would seek to make it a legislated requirement that contracts to which a small business is party must be negotiated on request. This does not address any of the issues highlighted by this submission, particularly the power and information imbalances between small businesses and larger organizations. The SBDC does not believe that such an approach would deliver significant benefit to the small business sector. When considering this in light of the costs of implementing legislative reform to this effect, the SBDC does not believe it would assist the Federal Government in achieving meaningful outcomes in resolving this issue.

### **The SBDC supports Option 3**

The SBDC, in line with the Federal Government's position, supports the implementation of Option 3, which is to extend the unfair contract term provisions to small business contracts through legislative amendment. The SBDC supports the extension of this provision to all contracts to which a small business is party to; including where the small business uses such contracts for the supply or acquisition of goods and services.

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<sup>19</sup> Ibid 6

<sup>20</sup> Ibid 6, Page 157

Whilst the SBDC acknowledges that such a wide-reaching provision may create additional cost for small businesses, we believe that it will be outweighed by the expected benefit that may arise from this reform. It is likely that this provision will cause expense for small businesses that offer their clients standard form contracts as they have to spend time learning about the change as well as potentially removing any unfair terms from their own standard form contracts. However, this is likely to be a one off burden and expense. On the other hand, if the provision only applied to some small business contracts it could cause more confusion as small businesses have to continuously consider whether the provision applies to their contracts.

## Issues to consider

### Applicability of the reform – defining small business

The most challenging aspect of this proposed reform will be determining the applicability of the provision, whether by using a definition of ‘small business’ or ‘small business transaction’. The SBDC believes that the overarching principle of this reform should be to provide protection to as many small businesses as possible and therefore the applicability criteria needs to be developed with this in mind. The legislative reform to extend the protection beyond individual consumers will require careful consideration to ensure that the resulting amendment provides certainty, is effective and creates minimal additional red tape.

In the SBDC’s opinion, it would be preferable to use ‘small business’ rather than a ‘small business transaction’ as the eligibility criteria for determining whether the legislative amendment applies. Using ‘small business transaction’ is problematic as transactions undertaken by small businesses are numerous and varied therefore capturing them using legislative instruments would be difficult. The other option for defining what transactions would be covered may be through the use of a monetary value, for example, only transactions valued above \$2000 are captured by the amendment. However, this would create a legal loophole and contracts could be structured to avoid being captured, for example by using an automatic rollover clause to extend the term of the contract (and therefore the actual monetary value of the contract) or breaking the price down into different components.

Small businesses account for 97.3%<sup>21</sup> of all businesses in Australia. Therefore, using a definition of ‘small business’ (rather than ‘small business transaction’) would ensure that the new protection applies more broadly across the sector. As discussed earlier, there is no standard definition of small business used across Government and regulators in Australia. The Productivity Commission, when examining regulator engagement with small business, commented that regulators, when developing a definition of small business for their purpose, must be clear about the problem or

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<sup>21</sup> Ibid 4

barrier they are attempting to overcome.<sup>22</sup> The SBDC believes that in this case the problem that needs to be addressed is the impact of unfair terms in standard form contracts on all small businesses and therefore the definition used must be inclusive, rather than exclusive.

The Productivity Commission succinctly described the variation in the features of the small business sector and concluded that it is “neither feasible nor appropriate to develop a single definition (qualitative or quantitative) of small business that would be suitable for all regulatory purposes”.<sup>23</sup> The benefit of the definition used by the SBDC Act<sup>24</sup> is that it does not exclude businesses based on arbitrary factors such as number of employees, annual turnover (which is not indicative of actual profit) or legal structure.

The SBDC believes that using the “factor approach” to defining small business is counterproductive and may create unintended consequences in the policy setting. Factors create circumstances in which a small business on the margins falls in and out of the legislative protection, for example as their turnover or employee size fluctuates. Such an approach could create artificiality in the marketplace as businesses could structure their affairs and contracts according to the criteria set out by the legislation. For example, if the legislative amendment applied to businesses with 20 or fewer employees then larger businesses may decide to enter agreements only with businesses with 21 or more employees, thus avoiding being captured by the legislation. The consequences of this will be far reaching to Government and to small and large businesses alike.

The discussion above illustrates the difficulty of developing eligibility criteria based on what is a small business. Perhaps then the solution lies in the development of a definition that excludes the applicability of this reform based on **what is not** a small business. Using this approach, the proposed amendment would apply broadly unless the business meets the criteria set out by the definition (for example, publicly listed companies). One benefit of this approach would be the disincentive it creates in the market place to include unfair terms in standard form contracts. A more powerful business may find it easier and more cost effective to remove all unfair terms as a business rule rather than include them and then face the legal costs and processes associated with testing whether the legislation applies to these contracts, rendering the unfair terms void.

The SBDC would recommend that the CAANZ develop a draft definition for the purposes of this amendment and seek feedback from key stakeholders on its appropriateness.

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<sup>22</sup> The Productivity Commission 2013 *Regulator Engagement with Small Business Research Report*, Canberra; Available from [http://www.pc.gov.au/data/assets/pdf\\_file/0007/128338/small-business.pdf](http://www.pc.gov.au/data/assets/pdf_file/0007/128338/small-business.pdf) [31 July 2014]

<sup>23</sup> Ibid 22, page 32

<sup>24</sup> Refer to page 3 of this submission for the definition

## Defining unfair

In relation to how the legislation should deal with what is “unfair” the SBDC believes that the current definition under the ACL should be adopted. Given the breadth of examples of unfair terms, the SBDC believes a definition of the characteristics of an unfair term is preferable to a running list, which would require updating regularly. This approach may create confusion amongst those impacted by the reform and could create loopholes for businesses that might exploit them if it is in their interests to do so.

In line with this, the SBDC would support the publication of a guide to educate those using standard form contracts about what constitutes an “unfair” term under the new provision. This should ideally include the publication of a list of real life examples and case studies, which should be updated regularly and supported by an extensive education campaign across the country.

## Avoid confusion and red tape

As with all legislative reform, the Government must consider the intended and consequential impacts new legislation will have on the sector being regulated. In this way, law makers must think about how the processes and documentation associated with such a reform will impact on the small business sector. Ideally, the reform would be implemented and run in such a way as to reduce the regulatory burden on small business while delivering maximum benefit to industry and the community. This may include transitional periods and should always be supported by appropriate information campaigns.

## Conclusion

The SBDC welcomes the opportunity to input to such an important review and applauds the Federal Government for its commitment to extending the protection against unfair contract terms in standard form contracts to small businesses.

As argued in this submission, the SBDC strongly supports reform of this area via Option 3 as it is necessary for the advancement of the small business sector in Australia. As with all reforms to legislation however, there needs to be corresponding enforcement of the legislation. In that regard the SBDC strongly recommends that the resourcing of the ACCC is reviewed in conjunction with the development of the proposed amendment. Effective change in this area requires the legislative backing as well as an adequately resourced regulator.

For further information please contact Ms Darcy Bosch (Senior Policy & Project Officer) on 6552 3308 or on [darcy.bosch@smallbusiness.wa.gov.au](mailto:darcy.bosch@smallbusiness.wa.gov.au)

\*Please note that this submission contains the opinions of the Small Business Development Corporation and not the Western Australian State Government