

COMMONWEALTH GOVERNMENT RESPONSE
TO THE
SENATE STANDING COMMITTEE ON ECONOMICS
REPORT ON

**THE NEED, SCOPE AND CONTENT OF A
DEFINITION OF UNCONSCIONABLE CONDUCT
FOR THE PURPOSES OF PART IVA OF THE
TRADE PRACTICES ACT 1974**

GOVERNMENT RESPONSE TO THE REPORT OF THE SENATE ECONOMICS COMMITTEE INQUIRY INTO THE NEED, SCOPE AND CONTENT OF A DEFINITION OF UNCONSCIONABLE CONDUCT FOR THE PURPOSES OF PART IVA OF THE TRADE PRACTICES ACT 1974

BACKGROUND

On 16 September 2008, following a motion from Senator Nick Xenophon, the Senate referred the following matter to the Standing Committee on Economics (the Committee) for inquiry and report by 3 December 2008:

The need to develop a clear statutory definition of unconscionable conduct for the purposes of Part IVA of the Trade Practices Act 1974 and the scope and content of such a definition.

Unconscionable conduct, a doctrine originally developed in the courts of equity, is conduct that attracts such moral opprobrium that it justifies the courts in granting relief to those who suffer by it. In *Commercial Bank of Australia v Amadio* (1983) 151 CLR 447, his Honour Justice Mason described unconscionable conduct as a situation where ‘unconscientious advantage is taken of an innocent party whose will is overborne so that it is not independent and voluntary ... [or who] is unable to make a worthwhile judgment as to what is in his best interest’.

Part IVA of the *Trade Practices Act 1974* (TPA) and Part 2 of the *Australian Securities and Investments Commission Act 2001* (ASIC Act) contain provisions incorporating this equitable doctrine, thereby providing access to an additional range of remedies for unconscionable conduct.

The Committee received 31 submissions, and held a public hearing in Sydney on 3 November 2008. The Committee’s report was tabled in the Senate by Senator Don Farrell on 3 December 2008.

The Committee’s report makes three recommendations. These recommendations are directed at clarifying the meaning of ‘unconscionable conduct’ in the context of section 51AC of the TPA. Section 51AC extends the prohibition of unconscionable conduct to transactions involving businesses, rather than simply consumers or individuals.

The Committee did not recommend a definition of unconscionable conduct, as it considered such a definition could create more uncertainty and confusion for the courts and have adverse consequences for the interests of consumers and businesses. Rather, the Committee suggested that its ‘precise and targeted [recommended] amendments will provide greater clarity for the courts and for all parties involved than an all-encompassing definition of ‘unconscionable conduct’’.¹

The Coalition senators on the Committee and Senator Xenophon made additional comments to the report. These minority comments made several recommendations concerning unconscionable conduct, including recommendations that would amend Part IVA of the TPA.

The Committee’s recommendations, and the Government’s response to each, are set out below. The minority’s comments are also addressed.

¹ page 43 of the report.

GOVERNMENT RESPONSE TO THE COMMITTEE'S RECOMMENDATIONS

Recommendation 1

The committee notes that the parliamentary Joint Committee on Corporations and Financial Services has just inquired into the Franchising Code of Conduct. Pending the response to this inquiry, the committee generally supports an amendment to section 51AC of the Trade Practices Act which states that the prohibited conduct in the supply and acquisition of goods or services relates to the terms or progress of a contract.

The Government **accepts** this recommendation.

The Government acknowledges the belief among some stakeholders that the courts have not been willing to tackle what is called 'substantive unconscionability'. Contrasted with what has been called 'procedural unconscionability', which is concerned primarily with the formation of contracts, substantive unconscionability would refer to situations where the terms of a contract, or behaviour by parties to a contract, attract such a high degree of moral opprobrium that to insist on the terms or engage in the behaviour would be unconscionable. Some submissions to the inquiry suggested that the courts focused too heavily on procedural unconscionability, which they argued is concerned only with the formation of contracts.

Section 51AC provides a number of factors which the court may consider in making a finding of unconscionable conduct. Those factors already implicitly acknowledge the significance of the terms and progress of a contract to a possible finding of unconscionable conduct. For example, the section refers to the parties' conduct towards each other, whether the contract provides for rights of unilateral variation, and undue influence or pressure as factors to which the court may have regard in making a determination of unconscionable conduct.

The Committee's findings suggest that these provisions may not have been accorded sufficient weight by the courts when testing section 51AC. Therefore, the Government agrees that an amendment to emphasise that the terms and progress of a contract are relevant to a finding of unconscionable conduct will help clarify the intention of Parliament. The Government will introduce an amendment to section 51AC (and section 12CC of the *Australian Securities and Investments Commission Act 2001*, which mirrors section 51AC) along the lines suggested by the Committee at the earliest convenient opportunity.

Nevertheless, so-called 'procedural unconscionability' will still be relevant to a finding of unconscionable conduct under section 51AC. The equitable principles that have developed in relation to unconscionable conduct continue to provide a strong basis for the operation of Part IVA of the TPA. The amendment to section 51AC will simply clarify the operation of the section and not alter the prohibition or create a new standard of business conduct.

On 2 October 2008, the Council of Australian Governments (COAG) agreed to the establishment of a new national consumer law, which will include a provision addressing unfair contract terms. Where a substantive term of a standard form contract is unfair, consumers may be able to use this provision to prevent the other party insisting on that unfair contract term.

The Committee noted the concerns of some stakeholders that:

the development of case law on section 51AC has been disappointing and that the section is therefore not working. In other words, there are many

more unfair contract terms ('substantive unconscionability') operating in Australia than what the prosecution record would indicate.²

The Government believes that the unfair contract terms provision agreed by COAG will address some of the concerns about 'substantive unconscionability' raised during the inquiry.

COAG agreed that the new national consumer law would be in place by the end of 2010. The Government introduced legislation on unfair contract terms into Parliament on 24 June 2009.

With regard to unfair contracts, the new provisions will not apply to business-to-business relationships. However, there are a number of ongoing processes examining the protections afforded to businesses in circumstances where they are dealing with other businesses with greater bargaining power and market power, including in the context of the Franchising Code of Conduct and the recommendations of this Inquiry.

The Government will consider the need for additional specific protections for businesses – including unfair practices and contract terms – when responding to specific identified problems. This is the approach taken by the Franchising Code review. Rather than offering general solutions to specific problems, this approach will avoid the risk of introducing uncertainty for franchising businesses and for those doing business in Australia more generally.

Recommendation 2

The committee recommends that the Federal Government engage industry participants from the retail tenancy and franchising sectors (among others) and the ACCC in an inquiry process. The inquiry should specifically consider the option of producing a list of clear examples, that all parties agree constitute 'unconscionable conduct', into the Trade Practices Act. Furthermore, the committee recommends that as a part of this national dialogue, a statement of principles should also be considered.

The Government **accepts** this recommendation.

An inquiry process would provide greater scope to examine stakeholder views on these options, and whether these options would address stakeholder concerns about unconscionable conduct or provide any greater clarity for Part IVA of the TPA.

The Minister for Competition Policy and Consumer Affairs will convene a panel of experts in the field of trade practices law and policy. That expert panel will engage in consultation with the Australian Competition and Consumer Commission (ACCC), retail tenancy and franchising industries, and small business organisations, as well as any other interested parties, in considering the need for a list of examples or statement of principles for Part IVA.

Further, the Government will ask the expert panel to consider the need to develop a list of specific behaviours that should be prohibited under the Franchising Code of Conduct. If the Panel considers that such a list would be appropriate for either Part IVA of the TPA or the Franchising Code, it will develop those lists, again in consultation with the ACCC and the relevant industries.

The panel's terms of reference are attached to this response. The Government intends for the panel to complete its work by the end of January 2010. The Government will consider the outcomes of

² page 8 of the report.

the inquiry process, including any suggested amendments to the TPA or the Franchising Code, when it receives the panel's final report.

Recommendation 3

The committee recommends that the ACCC pursue targeted investigation and funding of test cases.

The Government **accepts** this recommendation **in principle**.

The Government understands the desire for greater judicial guidance on unconscionable conduct under Part IVA of the TPA. While the decisions handed down by the courts since the introduction of section 51AC in 1998 have been instructive, a precise understanding of unconscionable conduct in the context of section 51AC has not been firmly settled. Further test cases concerning section 51AC could result in a more certain judicial understanding of the concept.

The ACCC is an independent statutory agency, responsible for determining its own enforcement priorities.

The Government notes that officers of the ACCC have made public comments recently which recognise the importance of establishing judicial guidance for the TPA. In giving evidence to the Committee, the ACCC noted:

the ACCC considers the case law as to the interpretation of sections 51AB, 51AA and 51AC is building ... and providing further guidance to market participants ... [T]he ACCC acknowledges the importance of judicial guidance in this area. In a speech to small business last July, [ACCC Chairman] Graeme Samuel noted the ACCC had from time to time taken matters through the misrepresentation provisions of the Trade Practices Act. He indicated that we would have, I guess, a renewed determination to pursue matters to the full extent in relation to both sections 51AC and 51AB. We have to do so in an environment when using taxpayers' money and being responsible as regulators that, where there are opportunities to settle matters outside of full hearings, we have to take that into account. That said, Mr Samuel was very clear in the importance of providing further guidance through the courts. We currently have a number of matters before the courts that we hope will provide further guidance in this very important area.³

In 1998 the ACCC was given directions (which are still in force) to initiate proceedings for the purpose of establishing legal precedents under section 51AC (see the Commonwealth of Australia Gazette, No. GN 35, 2 September 1998). The ACCC has indicated quite clearly that it is mindful of the importance of obtaining judicial guidance on Part IVA, and has factored this into its enforcement decision-making processes.

The Government encourages the ACCC to continue in its resolve to achieve further judicial guidance on unconscionable conduct under the TPA.

³ Evidence to the Senate Economics Committee, Parliament of Australia, Sydney, Monday 3 November 2008, page E9 (Mr Scott Gregson, General Manager, Coordination, Enforcement and Compliance Division, ACCC).

Further, the Government is committed to ensuring the ACCC has the enforcement tools necessary to administer the TPA effectively. The COAG agreement of 2 October 2008 provides for an enhanced range of consumer law penalties and enforcement tools. Where appropriate, these measures will be available for breaches of Part IVA.

On 24 June 2009, the Government introduced into Parliament the Trade Practices Amendment (Australian Consumer Law) Bill 2009. The Bill, when passed, will implement this enhanced package of penalties and enforcement tools for breaches of the unconscionable conduct provisions of the TPA.

Under the Bill the ACCC will be able to seek redress for people harmed by unconscionable conduct, without requiring those people to be parties to court proceedings. The ACCC will also be able to seek civil pecuniary penalties of up to \$1.1 million from corporations in breach of Part IVA, and will be able to issue infringement notices in relation to instances of unconscionable conduct. The ACCC will also be able to issue public warning notices about corporations suspected of contravening Part IVA, and will be able to seek disqualification orders to ban directors associated with findings of unconscionable conduct from managing corporations.

This enhanced enforcement regime will provide the ACCC with additional tools to bring proceedings under Part IVA. Further information about the Bill and the Australian Consumer Law may be found at www.treasury.gov.au. The Bill is currently being examined by the Senate Economics Committee.

GOVERNMENT RESPONSE TO THE MINORITY COMMENTS

[We] recommend that a definition of unconscionable conduct based on the approach taken by Associate Professor Zumbo, be inserted into section 51 AC of the Trade Practices Act and that it be made clear to the extent that it is not inconsistent with such a definition, the pre-existing common law and equitable principles should apply.

The Government **does not support** this recommendation.

As noted in response to Recommendation 1, the principles of unconscionable conduct as developed by the courts of equity continue to provide a strong basis for the operation of Part IVA of the TPA. The equitable prohibition is not merely a back-up for when the statutory prohibition fails. Rather, the equitable concept is intrinsically tied to the statutory framework, and it is the equitable concept which Parliament intended to incorporate into the TPA.

As the previous Government noted when introducing section 51AC, the:

new provision will extend the existing common law doctrine of unconscionability expressed in the existing section 51AA of the current act. The bill will use the expression ‘unconscionable conduct’ rather than ‘unfair conduct’ in order to build on the existing body of case law which has worked with respect to consumer protection provisions of the act and which will provide greater certainty to small businesses in assessing their legal rights and remedies.⁴

It would not provide any greater certainty to business to change fundamentally the concept of unconscionable conduct, as the Coalition senators and Senator Xenophon propose. The minority’s proposed definition, as the Committee noted, is too uncertain in law to provide any clarity for courts, consumers and businesses. It introduces concepts which are not synonymous with unconscionability as it is understood either in the law of equity or as it has been applied under the TPA (to the extent that there is any difference).

If inserted as a definition into the TPA, the Government considers that these concepts would substantively alter the nature of the prohibition of unconscionable conduct and lead to potentially greater confusion. The Government considers that inserting into the TPA a definition of ‘unconscionable conduct’ based on the minority’s proposed approach is not desirable.

⁴ *Commonwealth Parliamentary Debates*, House of Representatives, Tuesday 30 September 1997, page 8765 (the Hon Peter Reith MP, Minister for Workplace Relations and Small Business).

Associate Professor Zumbo has provided the Committee with a draft of a statutory list of examples of what constitutes unconscionable conduct based on s 51AC(3) ... We would recommend that Associate Professor Zumbo's draft be used as the basis for the enactment of a list of examples of conduct that constitute unconscionable conduct, recognising that such a list should not be considered exhaustive.

The Government **notes** this recommendation.

The Government has accepted the Committee's recommendation of an inquiry process to consider the issue of a statutory list of examples of unconscionable conduct. It would be inappropriate to pre-empt the outcome of that process.

The Government will consider the outcome of the inquiry process when it receives the expert panel's final report.

[We] recommend that the Trade Practices Act be amended to prohibit bullying, intimidation, physical force coercion and undue harassment.

The Government **does not support** this recommendation.

There are a number of laws at the Commonwealth level already in place which address this behaviour. For example, as the minority notes, section 60 of the TPA prohibits physical force, undue harassment and coercion in the context of consumer transactions. Furthermore, section 12DJ of the ASIC Act applies the same prohibition in a financial services context.

Where the conduct in question is so egregious that even in a robust business context it becomes bullying, intimidating, harassing or coercive, it is likely that state and territory criminal provisions may provide a remedy for affected individuals, as well as laws dealing with specific issues such as trespass and debt collection. The courts have also recognised that duress, including economic duress in some circumstances, can render a contract voidable.

Further, section 51AC already refers to undue influence or pressure being exerted on the parties as relevant to a finding of unconscionable conduct. There is no evidence at this time that all these potential legal remedies provide inadequate protection against bullying, intimidation, physical force, coercion or undue influence.

[We] recommend that a statutory duty of good faith be inserted in the Trade Practices Act and that it apply to all business to business relationships.

The Government **does not support** this recommendation.

There is some discussion in academic and business circles about the appropriateness of a general duty of good faith in business relationships. The Government does not consider that there is a sufficient policy basis for making such a broad change to the legislative framework governing all business relationships in Australia.

As the additional comments observe, the Joint Parliamentary Committee on Corporations and Financial Services recently recommended a duty of good faith in the context of franchise agreements. The Government is responding to this specific recommendation in the context of the Joint Committee's report.

[We] believe that the current Victorian legislative framework for dealing with unfair contract terms in consumer transactions should be extended to cover business to business relationships involving small businesses.

The Government **notes** this recommendation.

As noted in response to Recommendation 1 above, COAG has agreed that the new national consumer law will contain a provision dealing with unfair contract terms in standard-form contracts. The Government is considering the issue of unfairness in business-to-business contracts in the context of Recommendation 2 as set out above and its review of the Franchising Code of Conduct.

MINISTER FOR COMPETITION POLICY AND CONSUMER AFFAIRS' EXPERT PANEL TO ADVISE ON STRENGTHENING THE FRANCHISING CODE OF CONDUCT AND THE UNCONSCIONABLE CONDUCT PROVISIONS OF THE TRADE PRACTICES ACT 1974

BACKGROUND

Unconscionable conduct

- Unconscionable conduct is a judicially-developed concept, originating in the courts of equity, which allows the court to see that justice is done where unconscientious advantage is taken of an innocent party. The equitable concept is incorporated into the *Trade Practices Act 1974* (TPA) by section 51AA, and this is augmented by section 51AB and 51AC, which introduce general statutory duties not to engage in unconscionable conduct in dealing with consumers or other businesses. These provisions are set out in Part IVA of the TPA.
- On 16 September 2008, the Senate asked its Standing Committee on Economics to consider 'the need to develop a clear statutory definition of unconscionable conduct for the purposes of Part IVA of the *Trade Practices Act 1974* and the scope and content of such a definition' (Unconscionable Conduct Inquiry). The Committee presented its report on 3 December 2008.
- While the Committee did not recommend the introduction of a statutory definition of unconscionable conduct, it did make three recommendations aimed at clarifying the operation of section 51AC of the TPA without compromising the wider legislative framework. The Committee recommended that:
 - an amendment be made to section 51AC stating that the prohibited conduct in the supply and acquisition of goods or services relates to the terms or progress of a contract (Recommendation 1, page 36);
 - the Government engage the Australian Competition and Consumer Commission (ACCC) and industry participants from the retail tenancy and franchising sectors (among others) in an inquiry process, to consider the option of introducing a list of examples that all parties agree constitute 'unconscionable conduct', or a statement of principles, into the TPA (Recommendation 2, pages 38-9); and
 - the ACCC pursue targeted investigation and funding of test cases (Recommendation 3, page 39).

Franchising Code of Conduct

- On 1 December 2008 the Parliamentary Joint Committee on Corporations and Financial Services tabled its report on the Franchising Code of Conduct (Franchising Inquiry). The Joint Committee had inquired into the operation of the Code, with a view to identifying justifiable improvements.
 - The Joint Committee recommended (at Recommendation 8) the introduction of a general duty of good faith in relation to all aspects of a franchise agreement.
- While the Government considers that such a general provision would introduce uncertainty into the Code, it considers that there is merit in defining certain behaviours by parties to

franchise agreements that are inappropriate. These more defined concepts could be inserted into the Code as clear prohibitions for franchisees and franchisors.

TERMS OF REFERENCE

- In responding to these inquiries, the Government asks the Panel to consider the matters raised in Recommendation 2 of the Unconscionable Conduct Inquiry, and Recommendation 8 of the Franchising Inquiry, in accordance with the terms of reference below.

The Panel will:

- inquire into and report to the Minister for Competition Policy and Consumer Affairs on the need to introduce a list of examples that constitute ‘unconscionable conduct’, or a statement of principles, into the TPA;
- as part of this process, take account of the views of the ACCC, the retail tenancy and franchising industries, small business organisations, and such other parties as the panel considers would have an interest in the outcome of this process;
- consider the efficacy of a statutory list of examples or statement of principles concerning unconscionable conduct, and their legal effect;
- provide advice on whether the measures suggested by Recommendation 2 of the Unconscionable Conduct Inquiry would serve to: improve the clarity of Part IVA of the TPA; increase the effectiveness of those provisions; and improve community confidence in the effectiveness of those provisions; and
- if the Panel is satisfied that a list of examples or a statement of principles would improve the effectiveness of Part IVA, compile a list of examples that are generally accepted to constitute ‘unconscionable conduct’, or a statement of principles, having regard to the matters set out in these terms of reference.

The Panel will also:

- inquire into and report on the need to introduce into the Franchising Code of Conduct a list of examples of specific behaviours that are inappropriate in a franchising arrangement, with particular reference to:
 - unforeseen capital expenditure;
 - unilateral contract variation;
 - attribution of legal costs;
 - confidentiality agreements; and
 - franchisor-initiated changes to franchise agreements when a franchisee is trying to sell the business; and
- consider the potential impact any proposed measures could have on the franchising sector.