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Strengthening protections against unfair contract terms

The Australian Institute of Credit Management (AICM) welcomes the opportunity to contribute to the consultation on draft legislation to reform unfair contract terms.

AICM represents over 2,600 credit professionals who contribute to a resilient economy and drive successful business outcomes through:

- mitigating risk;
- maximising growth; and
- applying sound credit principles and practices.

Without our members, businesses are exposed to reputational damage, poor cash flow management and inefficient processes. Their employers are at risk of breaching regulatory requirements and not getting paid for hard won sales and services delivered.

Our members are the custodians of cash flow. They assess credit risk in all sectors and manage credit terms for the supply of goods, services and finance.

AICM members support reform that enables all businesses to engage in fair and efficient contractual arrangements including ensuring small businesses are not at a disadvantage as a supplier or customer in credit arrangements.

The principles that underpin an unfair contract term are supported by members and provide clear guidance on how to balance interests of the credit provider, namely a clause is an unfair term where it:

- causes a significant imbalance in the parties' rights and obligations;
- is not reasonably necessary to protect the legitimate interests of the party who would be advantaged by such terms, and
- would cause detriment (financial or otherwise) to a party if the term were to be applied or relied on.

These principles are used by AICM members to draft contract terms and guide actions where a dispute requires enforcement of rights under a contract.

AICM members are concerned that the draft legislation does not balance the impacts on the majority of credit providers who are applying the principles against the need to penalise the minority who are abusing their superior bargaining position resulting in unreasonable detriment. We expand on these concerns below.

Pecuniary penalty's

While not opposed to penalties where unfair terms cause unreasonable detriment when a party enforces an unfair term or there is evidence of clear intentions to rely on an unfair contract term, AICM members are concerned that potential penalties for mere existence of an unfair term could impact the efficiency of contractual arrangements. Specifically, where:

- It is not reasonably efficient for a supplier to have custom contracts or multiple versions of contracts to meet varying needs of their customer base, especially high-volume low value businesses.
- A term is not required for initial supplies to a customer but may be required for future supplies with that customer.

In these scenarios suppliers achieve efficiencies by including terms that may not be needed in all arrangements but are required in a relevant section of their customer base or supplies. These efficiencies ensure customers can access the supplies on favourable credit terms. Specifically, for small businesses it ensures they can access the supplies on credit terms without delay and expense associated with contract negotiations or paying before delivery.

Additionally, customers actively seeking to avoid their obligations are likely to use potential penalties to obtain an advantage despite the term not being relied on.

The consequences of not addressing the above could include some credit providers choosing not to extend credit terms to certain customers. For small business, this has the potential to offset the intention of the reform by increasing the disadvantages of small business compared to large businesses where favourable credit terms will be available.

Small business contract if one party employs fewer than 100 employees or turnover of less than \$10,000,000

AICM members note that monitoring of thresholds for small business is significantly complex and frustrating due to the lack of publicly available information to verify company size.

The lack of financial information creates barriers and inefficiencies for small business access to credit.

The AICM provided extensive background to these issues in a submission to the 2018 changes to reporting thresholds¹ in conjunction with the Australian Finance Industry Association (AFIA) and the Australian Restructuring Insolvency and Turnaround Association (ARITA).

¹ https://treasury.gov.au/sites/default/files/2019-04/c2019-t342318-afia_aicm_arita.pdf

AICM members recommend considering a change to the threshold following a review of any reforms to ensure the appropriate balance has been achieved. This will ensure any unintended consequences, such as reduction in credit terms offered to small businesses, are minimised.

Extending penalties and remedies to other suppliers and contracts

AICM members are concerned that contract terms may be deemed unfair where they are the same or substantially the same as another term without reference to the specific situation or if the term was relied upon.

While a positive outcome of this reform is encouraging removal of unfair terms from contracts where they aren't reasonably necessary, AICM notes that most members organisations have updated standard form contracts and this extension is likely to result in:

- Customers challenging a term that is reasonably necessary due to the specific nature of the relationship which creates inefficiencies and costs for the supplier to address.
- Customers challenging a term included to cover potential future supplies, but the supplier has not relied on the term or caused detriment.

AICM members expect this to frustrate collection of valid supplies where the principles of unfair contracts have not been breached purely due to a customer actively seeking to avoid their payment obligations.

- Costs being incurred to defend the use of the term in court by demonstrating the different circumstances that apply and the reasonableness of the term.

In summary, AICM members support the intent of the reforms but strongly recommend the reform limit application of penalties to circumstances where the principles of the unfair contract terms regime are breached, and the term has been relied on or there is clear intention to rely on the term.

Additionally, the actual circumstances of each occasion where a term is used is considered before penalties apply or a term is deemed void.

Finally, the AICM has been working in consultation with the Australian Credit Forum (ACF) on its submission and intends to provide further comment after consultation with ACF members on Tuesday 21 September 2021 which will provide further insight to the impacts of the concerns noted in this submission.

We welcome the opportunity to further contribute to the discussion of the reforms.

Yours sincerely

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Australian Institute of Credit Management