

Article Information

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Time to play fair! Unfair contract terms regime extended to small businesses

Long gone are the days of “the contract is the contract”. Whilst many of us have always taken a “balanced” and “plain English” approach to drafting contracts

The Government has decided that there is a need to introduce laws to now make sure that businesses take this approach.

Will the new laws affect you?

You will hear people talk about “standard form contracts” and “small business contracts” but what are these?

Only one party to a contract needs to be a small business for the new laws to apply. A contract will be a “small business contract” if any party has less than 20 employees and the upfront amount payable under the contract is under \$300,000, or where the contract is longer than 12 months, \$1 million.

What do you need to do?

Your contracts and other related documents (e.g. manuals, guidelines etc.) will need to be reviewed from a fairness perspective.

Internal processes will also need to be reviewed.

You can approach this in 2 ways - determine case by case if the new laws apply and use the appropriate contract or you could apply the new laws to all your contracts. As to which approach you take will depend on your business and who you deal with.

Depending on the approach you take, you may need to introduce a process by which you assess any new contract or renewal or variation to an existing contract, to determine whether or not the new laws apply.

And again, whilst many of us have always taken the approach during the negotiation process of considering any request for changes to a contract and if the answer is “no” giving an explanation, the new laws signal an end to anyone taking the “take it or leave” approach.

When do you need to do this?

Although we have 12 months within which to make any changes, we recommend starting the process now.

Are the new laws a good thing?

We think so.

You can still include terms in a contract which have been the subject of commercial negotiation and/or legitimately protect your interests.

All the new laws mean is that your contracts need to be “Plain English” and easy-to-read and cannot include, for example, one-sided termination or unilateral variation clauses, unfair indemnity and release clauses and other “unreasonable” terms.

It may help to think about your contracts in terms of, if you were the other party to the contract how would you feel about

the terms in those contracts?

What happens if there is an “unfair term” in your contract?

Any such term will be void. If there are any terms you decide to keep in your contracts which are “line-ball”, then special care needs to be taken with drafting to make sure that, if on challenge the term found to be unfair, this does not result in other clauses in the contract being inadvertently affected, that is also void.

The following is a quick summary of the new laws:

Introduction

New laws will apply from 12 November 2016 that will extend the operation of the unfair contract terms protections to small businesses that enter into, renew or vary standard form contracts. Under the new regime, a contract is a “small business contract” if:

1. at least one party is a business that employs fewer than 20 persons
2. the upfront price payable does not exceed either:
 1. \$300,000, or
 2. \$1,000,000 where the contract is for more than 12 months
3. the contract is a standard form contract for the supply of goods or services, or a sale or grant of an interest in land.

An unfair contract term can be declared void and the contract may only continue to bind the parties if it can operate without the unfair term.

Although the aim is to provide protection for small businesses, it is clear that many medium or large scale businesses may also be covered by the new protections.

Calculation of employees

In counting persons employed by a business, each full-time, part-time and casual employee constitutes one person. Casual employees that are employed on a regular and systematic (rather than seasonal) basis are to be counted.

Contracts that may be captured

A variety of small business contracts may be captured by the new protections (subject to any contracts that may be prescribed and exempted in the future). These may include:

- standard small-business to small-business contracts
- franchising documents (e.g. franchising agreements, disclosure documents, and operating and procedures manuals)
- distribution or supply arrangements
- retail leases.

What is an unfair term?

A term is unfair if it:

1. would cause a significant imbalance in the parties’ rights and obligations
2. is not reasonably necessary in order to protect the legitimate interests of the party who would be advantaged
3. it would cause financial or other detriment to the other party.

Examples of unfair terms

Terms that may be considered unfair include where one party (but not the other) can:

- avoid or limit the performance of the contract
- terminate the contract
- vary, renew or not renew the contract
- unreasonably requests security that is above and beyond what is necessary
- rely on a restraint of trade clause that is not reasonably necessary to protect legitimate business interests.

Practical recommendations

Over the next 12 months, we recommend that businesses entering into small business contracts review their standard form

contracts to ensure compliance and best practice.

Our practical recommendations include:

- removing any terms which may be unfair – fairness and transparency in your dealings will enhance contractual certainty and confidence, and develop your reputation and commercial relationships
- undertaking appropriate due diligence for high-value transactions to reduce any future compliance cost
- at the time of entering into the contract, confirming an employee count, or that the business employs fewer or more than 20 employees where this is not in issue
- having alternative dispute resolution procedures to resolve disputes around unfair contract terms
- seeking legal advice about whether it is appropriate to use a standard form contract or moving to a negotiated contract for some transactions.