

# *Spier Consulting - Legal*

## **Submission to the Senate Economics Legislation Committee concerning Treasury Legislation Amendment (Small Business and Unfair Contract Terms) Bill 2015**

I am fully supportive, in principle, of the Commonwealth Government's proposal to extend Unfair Contract Term (UCT) protections to small business.

Many small businesses are subject to UCT's in the standard form contracts which they enter into with larger businesses. I often represent small businesses or their associations and see many of the issues.

### **Background**

In May 2009 the then Minister for Consumer Affairs, the Hon, Chris Bowen MP issued draft legislation to prohibit unfair contract terms.

The proposed law covered business to business and well as consumer to business contracts. The initial proposal had no threshold in relation to contracts covered by the proposed legislation.

In relation to business to business contracts the then Minister said,

“Standard-form contracts are used by parties irrespective of the legal status or nature of the party to whom the contract is presented, and without any effective opportunity for that party to negotiate the term. In such cases, it would be invidious to suggest that the same term, which may be considered unfair in relation to a contract entered into by a natural person, would not be similarly unfair in relation to a business, where neither of them is in a position to negotiate the term”

After consultations the then Minister proposed that business to business dealings were to have a contract threshold of \$2 million.

However in the Bill that was eventually tabled in Parliament business to business contracts were excluded.

## The present

The Coalition went to the last Election promising business to business UCT legislation. The Minister for Small Business the Hon. Bruce Bilson MP embarked on an extensive consultation process proposing an extension of the current consumer provisions to small business contracts.

There is a general acceptance that the law is warranted but the critical issue is the threshold level where the law applies to business to business contracts.

The proposed legislation has the following thresholds,

- Businesses with less than 20 employees ,and
- The **upfront price payable** under the contract does not exceed \$100,000; or
- The contract has a duration of more than 12 months and the **upfront price payable** under the contract does not exceed \$250,000.

There is no differential between services or goods or combinations of goods and services. Small businesses who buy goods or acquire goods and services for resale will quickly pass the thresholds. Small businesses who acquire services only are more likely to fall within the proposed thresholds.

The “upfront price payable” under the contract is defined in the Australian Consumer Law as the consideration that:

- a) Is provided, or is to be provided, for the supply, sale or grant under the contract; and
- b) Is disclosed at or before the time the contract is entered into;

But does not include any other consideration that is contingent on the occurrence or non-occurrence of a particular event.

In my view the thresholds are somewhat low and will exclude many small business contracts and particularly those with main suppliers and main customers which involve goods or goods and services,

The larger suppliers will often be the most difficult yet might fall outside the threshold. On the other hand small suppliers with less clout will fall within the threshold.

Consequently if the two categories use the same possibly unfair terms, which is quite possible, one will be struck out, the other will not.

A related issue is that what constitutes an “upfront price payable” in small business contracts is problematic. The definition is taken from the business- consumer regime

and not the business to business where there are a variety of fees and costs. As a result the thresholds are readily reached.

I suggest that the Committee consider the current monetary thresholds and consider whether they are appropriate for what is intended by the proposed legislation.

To assist the Committee I list some other thresholds by way of comparison.

- The CCA collective bargaining regime has different thresholds depending on the sector starting @ \$ 3 million annual dealings, then \$5 million for farmers, \$10 million for agricultural machinery, \$ 15 million for fuel resellers and rising up to \$20 mill for new car dealers.
- The proposed Small Business and Family Ombudsman, 100 employees.
- CCA Unconscionable conduct, none.
- CCA Unfair contract terms for consumers- none.
- CCA Small business purchases re warranty protection - \$40,000 for any individual purchase e.g. photo copier.

### **“Up front Price payable” – UCT Bill**

The upfront price payable means the amount that is disclosed to the other party at or before the time the contract is entered into. This means any future payments will be included in the upfront price provided they are disclosed to the small business in a transparent way (e.g. it is made clear on what basis such payments would be determined) at or before the time the contract is entered into.

However, the upfront price will not include any amount that is conditional on an event happening or not happening. For example, terms that impose additional fees or charges as a consequence of the other party breaching or exiting during the period of the contract would not be included in the upfront price.

The upfront price is arguably the known price or likely price at the time of entering into the contract. It is likely that in the future suppliers will put into a contract. the likely price or at least the minimum annual price or the likely price over the whole contract. A classic area is franchising.

It is confusing what the ‘up front price payable ‘actually covers and small business wants that to be clarified as it is likely that bigger businesses will use that confusion.  
**For example.**

An example of the confusion with what will form the upfront price is highlighted by the following typical payments seen in a franchise agreement (assuming it is considered to be a standard form contract):

An upfront fee for the grant of rights - this would be included.

An ongoing franchise fee may form part of the upfront price unless it is considered "contingent". Many retail and service franchise agreements are based on a fixed percentage of gross sales (revenue or profit) for a particular trading period. Some agreements may have a minimum specified amount such as \$1,000 per month or a combination of both (e.g. the greater of 6% of Gross Sales or \$1,000). Those minimums may also be subject to review by CPI increases or another review mechanism which could be contingent.

Other payments typically appear including a contribution to a marketing or cooperative fund controlled by the franchisor. It is usually calculated in a similar way to an ongoing royalty however but should a payment of that kind be included in the determination of the upfront price when it is essentially for a cooperative purpose.

There is also usually a "renewal fee" which is typically paid before the end of the term of the contract to secure a renewal, a transfer fee (usually based on a percentage of sale price).

Many franchisors also control premises by holding the lease (or an associate holding the lease) which are leased or licensed by franchisees. Typically the rent and outgoings are "passed through" at the cost to the franchisor however those payments can be significant.

Whilst they are usually part of a separate outlet licence agreement there is potential for a franchisor to include the obligation to pay in a franchise agreement (with the effect that the value of a good or service supplied is higher) to get over the threshold. The same may apply to the acquisition of assets such as an existing franchise business as a going concern in concert with the supplies made under the franchise agreement. It is not uncommon for franchisees to acquire other goods and services through the franchise agreement from a franchisor (or associate). It will be necessary to determine if those amounts form part of the upfront price.

These examples of obligations to make payments during the course of the term of the agreement can complicate the process of determining if they are considered in or out of the upfront price.

It is not clear if those payments are "contingent" because they are dependent on the sales occurring yet they are disclosed and known.

**As stated earlier the upfront price payable is taken from the consumer provisions but there is no threshold in relation to those. Up front price payable has a different purpose there.**

This issue demonstrated above is common in different ways to many contracts. "Up front" does not appear to be only up front but all known payments during the life of the contract.

**It may be that in relation to business to business contracts the payments for the ongoing supply of the goods and/or services that are the basis of the contract should be excluded from the definition of "up front".**

### **Impact of thresholds in relation to various businesses.**

- Grocery stores

A medium size independent grocery store will have many suppliers but there will be one main one, Metcash, the grocery wholesaler.

Purchases from Metcash in groceries will be many millions annually, no matter the size of the store. In addition, in many States Metcash subsidiary will supply liquor products, and again in the millions annually.

Other major suppliers to grocers will be poultry suppliers, dairy products, bakers, all will in most cases be in the millions annually, not to mention rent and utilities.

Many of the supply contracts will be for more than one year. Metcash contract, for instance, is for 5 years.

In many cases it will be known at the outset what minimum monthly purchases will be and not doubt that is part of the 'up front price payable'

- Newsagencies

A small suburban newsagency might spend some \$250,000 annually on magazines, spread over three suppliers but two dominate. Newspapers and phone cards will be around the \$100,000. As will rent.

Most of the supply contracts will be for more than one year. Again there will be known monthly minimum spend.

- Hotels.

Most will have more than 20 employees and annual contracts with suppliers such as Fosters, Lion and liquor wholesalers will be over the thresholds. Again there will be known monthly minimum spends.

- Petrol resellers

Where the service station operator buys the fuel the annual amount will in most cases be many millions. Again known minimum monthly spends.

### **What might the transaction threshold be?**

There are many options. The monetary thresholds might be higher or that there might be a higher threshold for contracts involving goods and contracts involving goods and services. There is even a valid case for no transaction threshold as the issue of what is “unfair” has its own threshold.

An argument against the higher threshold is that so called high value contracts should involve legal advice. That might be good advice in theory but from my experience no matter the level of legal advice and the size of the contracting parties, the “take of leave” regime still dominates.

I suggest the following possible alternative options.

- An overall threshold of \$2 million in line with the Government’s small business tax concessions thresholds,
- A simple doubling or trebling of the proposed thresholds.
- Exclude from the definition of ‘up front price’ payments for the ongoing supply of the goods and services which are the basis of the contract.

Whichever transaction threshold is “adopted” I suggest that the legislation be reviewed in two years time.

### **Other issues**

#### The definition of ‘up front price payable’

As indicated I have some concern about the definition of “up front price payable” in relation to the monetary thresholds. The essential issues is how in the ‘up front price payable’ calculated.

Hopefully the ACCC can assist by way of guidance. An example of the upfront issue is the payment of franchise fees where various fees in addition to the ongoing franchise are payable and hence the threshold are quickly reached.

The upfront price payable is taken from the consumer provisions but there is no threshold in relation to those. Up front price payable has a different purpose there. See the next paragraph.

#### *The “upfront price” of the goods or service is exempt from the UCT law.*

This is an important issues for business, especially small business. Whilst at the outset of a contract when there has been a choice whether to enter into the contract or not such exclusion is understandable.

The exclusion should not apply upon renewal of a contract where one party is then in a captive situation.

#### *The “main subject matter” of the contract is exempt.*

Same comments as those above and what if the supplier /Customer changes the main subject matter

*Contracts prescribed by law or contracts that mirror a mandatory Code may exempted by the Minister.*

There should be no such exemptions. Some argue that where mandatory codes exist the UCT law should not apply.

The problem is that Codes do not prescribe an entire contract and to exclude a sector on the basis of the existence of a mandatory Code, such as, franchising, causes anomalies.

I would be happy to discuss any aspect of this submission. I am not claiming any confidentiality.

Yours truly,

***Hank Spier***