



***Australian Equipment Lessors Association
Leasing Technical Conference Sydney***

***“Commercial Unconscionability & The Trade
Practices Act”***

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Presented by

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1. INTRODUCTION

I greatly welcomed the opportunity to speak to this AELA Seminar. With my background in the private sector I am familiar with the important role your industry plays and the sound reputation of your Association in fostering good industry practices.

In this regard I have a great respect for the efforts of your long-serving Executive Director Ron Hardaker in contributing to policy developments central to the interests of the equipment leasing sector.

Today I will explain the role of the ACCC, the nature and scope of the unconscionable conduct provisions, and why they are important to fostering fair and competitive markets.

While business transactions have traditionally been subject to the common law and the Trade Practices Act, these laws were of limited relevance to the lease finance industry. Over recent years, however, laws that once only operated in protection of household consumers have been extended to cover business transactions.

These new legislative schemes apply to such aspects of the industry as disclosure, dispute resolution and remedies. A key aspect of this regulatory framework is the unconscionable conduct provisions of the Trade Practices Act.

Section 51AA was introduced to prevent large companies taking unfair advantage of smaller businesses, where the smaller business has a special disadvantage, such as illiteracy or a serious cognitive ability. The introduction of section 51AC in 1998 offers broader protection to small businesses in commercial transactions.

I note AELA's expression of concern in its 1999 – 2000 Review about prescriptive "business protection" measures and scepticism that "this type of legislation will achieve desired policy outcomes without unintended consequences".

An alternative "take" is that rather than being a negative for your industry, the new 51AC provision has synergy with one of AELA's key objectives; the promotion of ethical standards in dealings between association members and the general community. I would be interested to hear participants' latest views after an extended exposure to the provisions.

In discussing the relevance of the unconscionable conduct provisions, particularly section 51AC, to the equipment leasing and finance industry, I will

- address the new developments in this area of law, and the kinds of issues they have been generating.
- describe the approach taken by the ACCC in promoting compliance with the Trade Practices Act, in both enforcement actions and education, and finally,
- touch on the initiatives taken in terms of continued law reform in this area.

2. ACCC –HOW THE ACCC OPERATES

The object of the Trade Practices Act is to enhance the welfare of Australians with the promotion of competition and consumer protection through fair and informed markets. The role of the Commission is to apply the TPA properly without fear or favour, for the benefits of consumers of all kinds throughout Australian including:

- Household consumers
- Small, medium and big business
- Farmers
- Local State and Federal Governments

All Australian individuals and enterprises have an interest in being supplied competitively and efficiently at reasonable prices and where they are selling goods to sell to buyers who have to compete for their product. Through its Regional Offices in each State and Territory, the Commission ensures that it is close to where the real trade and commerce takes place.

Put in simple terms the TPA covers six broad areas:

- Restrictive trade practices – price fixing, market sharing, boycotts etc
- Anti competitive structures – acquisitions/mergers
- Unconscionable conduct
- Misleading and deceptive conduct
- Authorisation of potentially anti-competitive conduct where it is offset by public benefit
- Access and pricing regulation of utility sectors such as electricity, gas, telecommunications, airports and rail.

The Australian Competition and Consumer Commission has a dual role as:

- a national enforcement agency; and
- a provider of education and information for business and consumers in relation to compliance with the Trade Practices Act.

It is the first role that gains most publicity. But it is the information and support role, especially to small business, that secures wider business understanding and acceptance of good trade practices compliance.

Educative function of the ACCC

Since the 1998 government decision to strengthen the protection offered to small businesses under the TPA, the ACCC has upgraded the level and style of its dealing with small businesses, and implemented a strategy of small business outreach.

The activities of the Small Business Unit in the ACCC and the appointment of a Commissioner responsible for small business have also focussed on demonstrating to small businesses how to avoid or handle TPA related problems well before they require litigation.

The Small Business Unit has developed a considerable network of contacts for getting messages out to small business. The messages emphasise how understanding and compliance in relation to TPA matters reflects good management practice and hence assists business success and profitability. It is a pro-business message and one which has good effect.

It is not just a one-way process and the ACCC has also fostered consultation with business and professional representatives. This has included a Small Business Advisory Group that meets regularly under the Chairmanship of the Small Business Commissioner.

In the ACCC's experience, education and information support are key elements in ensuring compliance with the TPA, avoidance of problems and emphasising dispute resolution as a first option. This is particularly so when the subject matter is as complex as unconscionability. To this end, the ACCC Small Business Program has focussed on innovative and "user friendly" ways of getting this information and skills out to the small business communities.

Now the ACCC is developing some "high impact" ways to help people to understand the law of unconscionable conduct. This includes a video on the subject which has been well received by larger businesses as a useful training tool. In addition the Commission holds a twice yearly satellite broadcast panel forum which now reaches close to 100 towns in regional Australia.

Trends in small business complaints

Complaints and inquiries received by the ACCC continue to increase. Each quarter the Commission now receives over 2000 substantive complaints and inquiries from small business.

The number of complaints about unconscionable conduct in business transactions (s51AC) tended to plateau, with around 150 in a quarter. The ACCC is actively pursuing litigation in 10 matters relating to unconscionable conduct generally.

Complaints, investigation and enforcement actions by the ACCC under section 51AC have primarily been in mainly in four areas

- franchising,
- retail tenancy
- primary producers in their dealings with businesses further down the supply chain
- mortgage contracts and guarantees.

The unconscionable conduct provisions have implications for all commercial relationships, including those between an equipment lessor and financier, as well as the lessee and lessor.

3. UNCONSCIONABLE CONDUCT

What it Means

So what exactly is unconscionable conduct?

Unconscionable conduct generally refers to situations where one party to a transaction has a special disadvantage, and the other party is likely to know of this disadvantage. Where the stronger party takes unfair advantage of this inequality, they have engaged in unconscionable conduct. This traditional, equitable doctrine of unconscionable conduct is difficult to establish, due to the requirement to prove a 'special disability'

The Trade Practices Act prohibits unconscionable conduct in both commercial dealings and consumer transactions. Although the Act gives no specific definition of unconscionability, it makes reference to the common law meaning of the term as it has evolved through court decisions.

Factors recognised as tending to result in a special disability include ignorance of important facts known to the other party, illiteracy or lack of education, poverty, infirmity, drunkenness, or lack of assistance or explanation where these are necessary.

In addition to the relative bargaining strengths of the parties, factors that may now be taken into account in this respect are

- any unreasonable condition or pressure exerted by the stronger party not necessary for protecting their legitimate business and
- any applicable industry code.

The first, section 51AA, is a broad prohibition. To prove unconscionability, the weaker party in a transaction must establish that it was in a position of special disadvantage that the stronger party knew about (or should have known about) and that the stronger party took unfair advantage of the position.

The second, section 51AB, introduces a general duty to trade fairly in relation to consumers by prohibiting conduct which is unconscionable.

The third, section 51AC, is more precisely focussed. It specifically prohibits one business dealing unconscionably with another. It sets out specific factors the courts may consider. These relate to both bargaining strength and a sample list of circumstances where the smaller party was required to submit to unreasonable conditions.

It should be noted that while Parliament transferred responsibility for consumer protection in relation to financial services to ASIC, the ACCC retains the role of preventing unconscionable conduct in relation to financial services, including equipment leasing and finance.

51AA and 51AC Cases

Given the extent to which the AELA role and membership is connected with the financial sector it may be of interest to mention a Section 51AA case against taken against National Australia Bank and a S51 AB case against Esanda.

The NAB matter involved a company whose director was incapacitated due to illness. The NAB sought and executed a guarantee against the director's wife, who had power of attorney over his affairs. The court declared this conduct to be unconscionable within the meaning of 51AA.

The ACCC alleged NAB sought and enforced a personal guarantee for \$200,000 to cover loans to the husband's business, using the couple's home as security, and then withheld \$7,760 over and above the home mortgage amount, realised after the home was sold.

The ACCC alleged that when NAB sought Mrs Ashton's guarantee, it did not explain the nature or effect of the guarantee, or advise her that she should obtain independent legal advice. The ACCC also alleged that NAB knew the company was in serious financial difficulty but did not inform Mrs Ashton. A year later, NAB demanded payment of the company's debts to the bank secured by the guarantee. The ACCC alleged that enforcement of the guarantee resulted in the sale of the Ashton's family home and NAB required the entire sale proceeds to be paid to the bank.

In May this year the ACCC instituted Federal Court proceedings against Esanda Finance Corporation Ltd, Capalaba Pty Ltd trading as Nationwide Mercantile Services, and a number of individuals.

The allegations involved a consumer who obtained a personal loan for a motor vehicle from Esanda. It is alleged the consumer was subjected to physical force, undue harassment and coercion in breach of section 60 of the Trade Practices Act, and unconscionable conduct in the supply of goods to a consumer, in breach of sections 51AB.

The ACCC alleged Esanda and/or its agents

- used physical force to gain entry to the consumer's residence and repossess the motor vehicle, engaged in aggressive and excessive behaviour towards the consumer
- failed to specify the amount of arrears or method of calculation
- repeatedly observed the consumer or third party in or around their home
- visited the spouse of the consumer at her place of employment
- restricted access from the consumer's residence
- charged the consumer unreasonable amounts by way of collection fees
- made excessive contact with the consumer and
- acted contrary to a notice of demand given to the consumer.

The ACCC is seeking declarations that Esanda, Capalaba and the individuals breached section 51AB and section 60, as well as injunctions restraining them from engaging in similar conduct in the future.

Implications of Section 51AC

51AC has a much broader application against unconscionable conduct than the earlier provisions. Section 51AC applies in cases where the transaction price does not exceed \$3 million, and the party seeking a remedy is not publicly listed.

51AC basically provides that businesses shall not, when selling or purchasing goods or services, engage in unconscionable conduct. Some factors that the court may consider include (but are not limited to);

- The bargaining strength of each party
- Applying conditions which were not reasonable nor necessary to protect the legitimate interests of the larger party including
 - denial of legal rights or remedies
 - attempting to enforce any conditions irrelevant to the agreement
 - unfair pressure tactics
 - failure to disclose relevant information.
 - various forms of misrepresentation relating to the weaker party's knowledge or understanding, the state of the goods or services involved and the actual level of any liability.
 - misuse of technical breaches of contract in an oppressive way
 - attempting to contract out of the central purpose of an agreement

51 AC Cases

The new unconscionable conduct provisions of the TPA have been tested in three court cases brought by the ACCC, alleging unconscionable conduct under section 51AC.

Broadly speaking, the court outcomes have clarified the meaning of unconscionable conduct under the TPA. In addition there are two other tenancy matters now before the Courts in Adelaide and Brisbane.

The first case decided under 51AC dealt with a retail landlord, *Leelee*, the operator of a food court. In dealings with one of their tenants, the landlord withheld crucial information about changes to the lease agreement. The landlord also failed to honour existing terms of the contract, and would not allow them to transfer the lease.

The court declared that the landlord had acted unconscionably, and granted injunctions preventing any similar behaviour in the future.

In reaching a decision on whether a party has acted unconscionably in breach of 51AC, the court considered:

- the parties' relative commercial strengths;
- whether undue influence was exerted;
- whether the contract exceeded what was reasonably necessary for the legitimate interest of the supplier;
- the requirements of any applicable industry code; and
- whether there was evidence of disclosure, good faith and willingness to negotiate.

The *Leelee* decision provides a concrete example of conduct that will be regarded as more than just tough commercial behaviour.

The case of *Simply No Knead* dealt with disputes between a franchisor and some of the small business franchisees. The franchisor refused to consider complaints unless by mail, and would not agree to joint meetings with the franchisees. The franchisor also applied other conditions on the meetings that were found to be unreasonable, and threatened to withhold necessary business supplies unless certain conditions were complied with.

Simply No Knead withheld disclosure documents unless each franchisee gave written consent to renew the agreement, and also competed directly with the franchisees in a way that was calculated to harm their businesses.

The Court found this conduct to be 'unreasonable, unfair, harsh, oppressive and wanting in good faith' and identified the following types of conduct that will be taken into account under 51AC:

- the imposition of undue pressure and unfair tactics;
- a failure to negotiate; and
- a lack of good faith;

Another factor the court will consider in looking at a matter under 51AC is a failure to comply with a relevant industry code. The *Cheap as Chips* franchise was found to have terminated a franchise without following the procedures contained within the *Franchising Code of Conduct*. The court also declared that the franchise's director attempted to contravene the code by trying to prevent a franchisee from associating with other franchisees for lawful purposes, and was knowingly concerned in other contraventions.

Cheap as Chips was restrained from engaging in similar conduct, and ordered to provide franchisees with reasonable access to records, notify all current franchisees about the outcome of the proceedings, pay compensation, interest and the Commission's legal costs. The company also implemented a trade practices compliance program.

These cases have to some extent clarified the factors the court will take into account when examining an action under 51AC.

4. INDUSTRY CODES OF PRACTICE

One important way businesses can achieve more effective relationships within their industry is by the adoption of a voluntary code of practice. Section 51AC specifically refers to these codes, and the ACCC encourages such initiatives.

The ACCC continues to work with the film industry on the development of the Code Of Conduct for Film Distribution and Exhibition, which sets out acceptable terms on which major film distributors deal with independent film exhibitors. The code seeks to create a clear framework for negotiation of terms and dispute resolution.

A voluntary code has also been adopted by private hospitals and health funds. The main aim of the Code is to minimise disputes between hospitals and health funds. It provides for an independent dispute resolution process with final reference to the Private Health Insurance Ombudsman, and it is hoped that the Code will lead to improved negotiation processes between hospitals and funds.

The Federal Minister for Small Business, Peter Reith, launched The Retail Grocery Industry Code of Conduct in Melbourne on 13 September 2000. It is a voluntary code, membership of which is comprised of many major grocery producers, wholesalers and retailers. It sets out requirements for produce standards, contracts, labelling and packaging, acquisitions, and dispute resolution. There have been some teething problems with the Code and a claim by the National Farmers Federation that it lacks teeth. The newly appointed Code Ombudsman has confirmed shortcomings such as his lack of power to require parties to mediate and lack of protection from victimisation of complainants.

The aims of the **AELA Code of Practice** are consistent with those of many other voluntary codes. It is in the interests of all businesses to encourage fair and honest conduct by all industry participants. Compliance with all applicable legal requirements improves the credibility of the industry. And it is in the interests of all parties concerned that contracts be entered into on the basis of all relevant facts, and that they are clear and certain. An effective dispute resolution mechanism also contributes to business efficiency.

5. ASSESSMENT TO DATE

Factors for Industry to Consider

It would be a “King Canute” approach to think the unconscionable conduct “tide” can be reversed. There is a community acceptance that despite the common law and all the other provisions of the TPA, a “safety net” is needed for situations where the “un-level playing field” between small businesses and larger more sophisticated firms is subject to unreasonable abuse.

I would suggest a few reasons why the equipment leasing and finance industry should be supportive of a balanced approach to this issue:

- Although ensuring compliance with regulations such as 51AC can incur administrative costs, for larger companies it is part of good business practice to achieve this, and as good corporate citizens play their part in ensuring the market operates as effectively and fairly as possible.
- Small businesses are responsible for a significant proportion of economic activity, and comprise a large portion of the customer base for financiers and equipment lessors. Presumably a confident and thriving small business sector is good news for your industry.
- A larger business that consistently gets away with acting unconscionably towards its small business customers or suppliers could be gaining an unfair competitive advantage over large competitors acting fairly in their business transactions.
- Where such behaviour occurs in an industry it is often to the detriment of the industry as a whole unless the misbehaviour is addressed quickly.

Equally it is recognised that protections for small business are not panaceas and that the powers available to the Commission need to be applied with commonsense and consistency. Unsubstantiated or vexatious claims are quickly weeded out by Commission processes.

To the extent it is possible to gauge, there has generally been a positive response by larger businesses to complying with the new S51 AC provision. Many leading franchisors for example identify a marked cleaning up of adverse behaviour by fringe elements in that sector which has had to embrace not only the new provision but also the application of a mandatory code of conduct.

In another “hot spot” area retail tenancy, there are ongoing difficulties. Disputes are primarily handled in State/Territory jurisdictions which have differing approaches and a tendency in some for regulatory intervention to spiral. There is a growing consensus that a “good practice” national self regulatory code would provide greater consistency and certainty for both landlords and tenants and take some of the heat off individual jurisdictions.

Reform Issues

Good law is never set in concrete and is amended to meet changed circumstances and shortcomings. At the same time it is important for business certainty that this does not involve continual chopping and changing or ever escalating levels of regulatory intervention.

In this context Federal Parliament recently approved amendments to the Trade Practices Act which put the ACCC in a better position to handle issues affecting small business. The new laws fill in gaps the amendments passed in 1998. The changes not only enhance the role of the ACCC in responding to cases of unreasonable exploitation, they also recognise the benefits of more flexible access to the courts and state tribunals.

The amendments cover a range of elements:

The Court now has discretion to allow the ACCC to intervene in private proceedings brought under the Trade Practices Act where the issues are of public interest.

The ACCC now has the right to seek declarations on the operations of the Act by the Court. Previously the ACCC was only able to intervene in existing matters. Declarations are relatively quick and inexpensive, providing authoritative statements on the operations of the Act.

Small business will also benefit from the ‘drawing down’ of 51 AC or the unconscionable conduct provisions in the Act. This amendment will remove any doubt that States as well as the Commonwealth can use legislation in relation to unconscionable conduct.

The time for initiating an action under the TPA has been extended to 6 years after the breach (previously three years and in some cases two years).

- ACCC's right to take representative action and seek damages for third parties under the restrictive trade practices provisions of the Act (except the secondary boycott provisions Section 45 D& E) has been extended. Previously this was restricted to the unconscionable conduct and consumer protection provisions. This will allow the ACCC to assist small business in protecting its rights in relation to anti-competitive conduct such as price fixing by cartels of large businesses.
- Courts now have discretionary powers to ensure that compensating victims of a TPA breach is given a higher priority than recovering a fine or penalty.
- Maximum monetary penalties for a breach of the Consumer Protection sections of the TPA (Part V) have been increased to \$1 million for corporations and \$200,000 for individuals
- For mergers and acquisitions, the definition of a market will now include a substantial market in regional Australia.
- The Court will also be able to award an extended range of non-financial remedies including orders in respect of Probation , Community Service, Corrective Advertising and Adverse Publicity

These changes as a whole emphasise Parliament's recognition of the need to support small business against unconscionable and anti-competitive behaviour of larger organisations.

Over the past year there have been a series of other issues raised about the need for reform of the TPA including:

- the case put by ACCC Chairman Professor Allan Fels for criminal sanctions against extreme cartel /market fixing behaviour as provided for under competition law in the USA and UK
- strengthening the abuse of market power test to include an "effects" test
- providing the Commission with "cease and desist" powers and
- in respect of mergers and acquisitions, some arguing for a less stringent test to accommodate alleged global competition factors while others claiming the TPA should be "beefed up" to include divestiture powers.

The return of the Coalition Government in last Saturday's Election means that all these matters and no doubt others will be given an airing in the comprehensive Review of the Trade Practices Act announced during the Election campaign.

CONCLUSION

The impact of commercial unconscionable behaviour in business is destructive and costly for all concerned. The role of the TPA and the ACCC in no way rules out aggressive and innovative competition. Quite to the contrary, we see it as the path to prosperity. However, all businesses can benefit from practices which seek to avoid excessive conflict and deal reasonably with suppliers and customers.

The Equipment Leasing sector has achieved a good record in their dealings with small business. This can be re-enforced in your industry by:

- Adhering to the spirit as well as the letter of the unconscionable conduct laws even to the extent of promoting their virtues;
- Continuing to encourage corporate members to promote the AELA Code of Practice to all employees and interested parties and make compliance with the code a top corporate priority.

Thank you once again for this opportunity to speak to you. I am happy to respond to questions.