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Submission on the Ministry of Consumer Affairs Consumer Law Reform Discussion Paper

This submission:

- Addresses only the discussion on unfair contract terms¹;
- Does not support the introduction of these provisions into New Zealand consumer law on the grounds that they are unnecessary;
- Notes the serious and broad commercial uncertainty which would be created in the service sector by provisions of this kind;
- Comments on flaws in the as yet untested Australian Consumer Law provisions;
- Sets out remedies already available to New Zealand consumers under existing law;
- Recommends positive encouragement of pro-consumer contractual provisions which are consistent with good operating practice for traders who enter into long-term contracts with consumers.

This submission has been prepared for Les Mills New Zealand Ltd which operates the world-class Les Mills clubs in New Zealand.

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¹ Pages 30 – 34.

SUBMISSION ON UNFAIR CONTRACT TERMS

1. The general proposal

- 1.1 Comments are sought on a proposal to import into New Zealand law provisions relating to unfair contract terms similar to those in the Australian Consumer Law. Those provisions have been passed by the Federal Parliament but are not yet in force or adopted into state law. Although similar provisions have been in effect in Victoria, they are not yet tested in the broader Australian environment.
- 1.2 This submission addresses unfair contract terms in the context of long-term contracts – contracts which are typically characterised by significant supplier investment in response to a long-term commitment by, and benefit to, consumers. For contracts of this kind, certainty of contract is central to the supplier's commitment.

2. Does New Zealand need unfair contract terms legislation?

- 2.1 As the Discussion Paper notes², there is no clearly defined problem in New Zealand which indicates a need for unfair contract terms. In paragraph 6 it is submitted that some fundamental differences between New Zealand law and Australian law (at least as it predates the as yet untested Australian Consumer Law) already provide New Zealand consumers with remedies which are not necessarily available to Australian consumers.

Submission: New Zealand does not need unfair contract terms legislation. Any mischief which would necessitate these provisions can already be addressed by existing legal and judicial³ means.

- 2.2 Further, it is submitted that provisions similar to the Australian provisions would create great uncertainty in businesses which by their nature enter into long term contracts with their consumer customers. Typically these businesses are in the service sector. The example of fitness centres is the obvious one. Most of these businesses are able to commit to investment in the services they provide to their customers **because** they have the certainty of income provided by their members' commitment to a long-term contract. This enables them to offer their members prices which typically decline according to the length of a member's commitment, as an incentive.

3. Good faith provisions

² Page 34.

³ Including the resolution of disputes in the Disputes Tribunals: see paragraph 6.

- 3.1 The Discussion Paper also asks if a “good faith” element should be imported into the definition of unfair contract terms. The resounding “no” on this point should not be seen as a reflection on the intentions of the submitter, but is based on the lack of consistent interpretation and judicial support for “good faith” provisions⁴. It is probably fair to say that everyone has their own personal view of what is good faith. Case law demonstrates that insertion of a statutory “good faith” provision would inevitably reduce clarity, not increase it.

Response to question 5: good faith provisions should not be included in New Zealand statute law but should be left for good traders to follow in their dealings with consumers.

4. The Australian provisions

- 4.1 The Australian provisions are attached to this document for reference⁵. The basic structure is this:
- (a) A term in a standard form consumer contract that is considered unfair is void – that is, the contract becomes silent regarding all matters relating to that term;
 - (b) It must be a term which causes an imbalance in the parties’ rights, is not reasonably necessary to protect one party’s legitimate interest and would be detrimental to the other party;
 - (c) The court must take into account transparency – is the term in plain language, legible, presented clearly and readily available to the affected party.
- 4.2 It is noted that the Australian unfair contract terms provisions envisages that standard form contracts have a real role in protecting a supplier’s legitimate business interests. However, the “grey” list of terms which “may be unfair”⁶ is likely to be taken by consumers as a list of terms which are prima facie unfair and thus challengeable. Indeed this is a reasonable consequence of the grey listing. A number of those terms are required in long-term contracts to protect suppliers’ legitimate business interests. See the example below at paragraphs 5.3 and 5.4.
- 4.3 One particular aspect of the Australian Consumer Law unfair contract terms provisions is that a term which is deemed to be unfair is **void**. That is, it is declared to have no effect and is removed from the contract. There appears to be no provision for the clause to be written down by the Court to achieve a result which appears to the Court to be fair. It is noted that precedent for adjustments of this kind are already

⁴ For an idea of the complexity of the issues involved and both (or all) sides of the debate, see the 145 pages of papers from the University of Auckland Faculty of Law’s *Commercial Good Faith* Symposium, 2005.

⁵ Copied from the Australian Consumer Law.

⁶ Australian Consumer Law s 25.

available in New Zealand statute law⁷ and also under the Fair Trading Act 1986 through its discretionary remedies.⁸

- 4.4 This uncertainty is exacerbated by the contents of the grey list of the Australian provisions, from which it is difficult to distil any single principle:
- (a) The grey list of terms is not expressed as being subject to s 24 but is presented as a stand-alone list;
 - (b) The terms in the grey list have not been subject to detailed ministerial scrutiny or at least a Regulatory Impact Analysis in New Zealand terms⁹. Each term should be separately considered. Within the list there are some terms which would be likely to be considered by New Zealand Courts to be inherently unfair and unenforceable because they purport to oust the jurisdiction of the court.¹⁰ There are other terms which are normal in long term contracts to give certainty in long term contracts;
 - (c) The Australian provisions are flawed in their focus, assuming they are necessary. It is apparent from the drafting of the provisions that it is envisaged that any consumer can challenge any contract, and it is up to the Court (or Disputes Tribunal) in each case to make a decision. The transaction costs of this are likely to be as considerable for the Courts or Disputes Tribunals as they are for the traders. Fair contract terms are likely to be re-litigated by consumers again and again, whether or not with the same trader;
 - (d) There is no positive standard in s 24. For example, s 24(2) requires the court to take into account the extent to which a term is transparent according to the criteria set out in s 24(3). There is no provision that says a term is fair if it is transparent, it is reasonably necessary to protect the legitimate interests of the party advantaged by it, and that detriment would be caused to a party if it were not applied or relied on. Yet this is the ultimate objective of good standard form contracts.
- 4.5 Further, it is noted that the Australian unfair contract terms provisions are not yet in effect. It seems unlikely that Australian consumers are significantly different from New Zealand consumers, and if this is the case. It is strongly suggested that if the Ministry is intent on imposing this untried legislation on New Zealand consumers, the Australian situation should be monitored for at least 2 years to assess the actual consequences.

⁷ Compare: New Zealand Illegal Contracts Act 1970 s 7(1): see paragraph 6.1(d).

⁸ Fair Trading Act s 43(2).

⁹ The Ministerial scrutiny is reserved for new terms.

¹⁰ Eg a term that limits or has the effect of limiting the evidence one party can adduce in proceedings relating to the contract: Australian Consumer Law s 24(1)(l).

5. **Consequences of a grey list of prima facie unfair terms**

- 5.1 It is not unreasonable for consumers who check up on their rights to consider a grey list of unfair terms to be a black list. This means that every standard form contract is challengeable if it contains at least one of the grey list terms, **regardless of whether the term is transparent, necessary to protect the legitimate interests of the supplier, and relied on by the supplier to preclude detriment.**
- 5.2 In addition, the focus on single unfair terms and the use of a grey list means that pro-consumer terms are not taken into account: the Australian approach does not entitle a Court to determine whether a contract **as a whole** is fair.¹¹
- 5.3 Just as one example: the grey list includes *a term which permits one party to terminate the contract*. In New Zealand the Consumer Guarantees Act already permits (and appropriately so) the consumer to terminate a contract when the goods or services substantially fail to comply with a guarantee. On the other hand a term which permits a supplier to terminate the contract unilaterally when the consumer has breached the contract would be subject to scrutiny by the Courts (or the Disputes Tribunal) which would have to decide whether it was fair in the circumstances.
- 5.4 If the Disputes Tribunal decided in a particular case that the term was not fair, the term would be void. It is likely that the decision would be published. Would the term then be void in all contracts? A fitness industry example would be a provision which permits a fitness club to terminate a member's contract in a number of circumstances, including where the member acts in a dangerous or offensive manner. Is the club then unable to exercise that term and exclude a dangerous member from the club?

Response to question 6: the approach used in the Australian Consumer Law of providing examples of unfair contract terms is not appropriate for New Zealand.

It is strongly doubted that it is appropriate for Australia, where it is as yet untested.

6. **New Zealand law already offers consumers greater protection**

- 6.1 New Zealand law already offers consumers considerable protection against unfair contract terms:
- (a) The Consumer Guarantees Act 1993 gives statutory rights which cannot be excluded by contract.¹² This gives consumers guarantees of performance and quality;

¹¹ See discussion on fair terms, paragraph 7.6.

¹² Eg *Price v Sports Marine Ltd* 24/5/96, Judge Hubble, DC Auckland NP2729/95

- (b) Section 9 of the Fair Trading Act provides consumers with remedies for misleading conduct in trade, including misleading conduct with respect to contract terms. This can be used to address terms which are not transparent, including fine print;
- (c) The Credit Contracts and Consumer Finance Act provides remedies for oppression in credit contracts;
- (d) Section 7 of the Illegal Contract Act 1970 gives courts the power to reopen and rewrite contracts which contain provisions which are illegal;
- (e) The Contractual Remedies Act 1979 gives consumers remedies where contract terms are misrepresented or where a substantial term of the contract is breached by the supplier;
- (f) The Contractual Remedies Act also preserves the equitable remedies of rectification and non est factum. Rectification is available to enable the terms of the contract to be altered so that they accurately reflect the parties' actual agreement. Non est factum is available where a party wishes to avoid liability under a signed document which contains very different terms from those it was represented to contain¹³;
- (g) The Contractual Mistakes Act 1977 permits a party to avoid a contract where it was entered into under mistake of fact.

6.2 The writer understands that many of these statutory protections are not part of the background of Australian federal or state law: the New Zealand Parliament in the 1970s and early 1980s took a very enlightened approach to reducing transaction costs in litigating contract-based disputes. For this reason alone, it is the writer's view that the Australian provisions should not be imported wholesale, if at all, into New Zealand consumer law.

6.3 Finally, we refer to the Disputes Tribunals Act and in particular sections 18 and 19 which give the Disputes Tribunals broad rights to address a dispute. Two provisions in particular are worth highlighting:

- (a) Section 18(6) provides:

The Tribunal shall determine the dispute according to the substantial merits and justice of the case, and in doing so shall have regard to the law but shall not be bound to give effect to strict legal rights or obligations or to legal forms or technicalities

- (b) Section 19(e) which provides:

Where it appears to the Tribunal that an agreement between the parties, or any term of any such agreement, is harsh or unconscionable, or that any

¹³ For a discussion on these see Burrows, Finn and Todd, *Law of Contract in New Zealand* 3d ed, 2007 pp. 290ff.

power conferred by an agreement between them has been exercised in a harsh or unconscionable manner, the Tribunal may make an order varying the agreement, or setting it aside (either wholly or in part);

- 6.4 When the Australian Productivity Commission visited the writer in 2007, its representatives commented strongly on the unitary jurisdiction of New Zealand and therefore its coordinated Disputes Tribunals, in comparison with the 9 different jurisdictions in Australia with Disputes Tribunals that operated to different statutory rules in each State. This should be borne in mind in assessing the significant differences between the Australian situation and the more coherent New Zealand situation.
- 6.5 In summary, it is difficult to see that there is a need for unfair contract terms provisions in New Zealand consumer law.

Response to Question 4: the inclusion of unfair contract terms provisions in the Fair Trading Act along the lines of the Australian provisions is not supported. New Zealand consumers already have remedies available to them in respect of unfair contract terms. The Australian provisions are untested. The regulatory impact of unfair contract terms has not been assessed even in Australia.

7. Principles based consumer law and principled traders

- 7.1 Frankly, it is difficult to see that the unfair contract terms provisions have any place in a principled consumer law in New Zealand. This submission has considered the unfair contract terms provisions in the context of the New Zealand legal framework which is different from the Australian legal framework.
- 7.2 Section 5 of the Discussion Paper addresses Principles-Based Law. In the introduction, there is reference to "ensuring that [the] essential pre-conditions for good decision-making exists and that an environment exists in which consumers can transact with confidence. When products or services do not live up to the expectations created by the information provided by the supplier, consumers can hold these suppliers to account." Indeed, this is the principle behind New Zealand's world-leading Consumer Guarantees Act (which has now been adopted by Australia in the Australian Consumer Law).
- 7.3 The corollary to this is that traders also need to be able to transact with confidence, while fulfilling consumers' reasonable expectations. If traders are not able to transact with confidence, this will necessarily be reflected in consumers' costs. This is particularly so in the case of long-term consumer contracts, where traders invest significant sums in response to the consumer's promise of continued support.
- 7.4 The paper Discussion Paper points out on page 25 "[Principles-based law] may be seen as loose and ineffective if affected parties do not

accept the principles and respond to the law by trying to minimise their compliance."

- 7.5 The concern of good traders who respect consumers and work hard to balance consumers' rights, while keeping costs down through the use of standard form contracts, is that they themselves do accept the principles of fair use of contract terms in standard form contracts – indeed it is central to a good long-term relationship with consumer clients.
- 7.6 However a prescriptive statutory approach like the as yet untested Australian unfair contracts terms provisions has negative consequences for good traders. It is likely to lead to advantage-taking by a category of consumers who for their own reasons wish to avoid their own (fair) responsibilities under the contract by one-to-one litigation through the Disputes Tribunals. This means that the efficiencies which should be able to be passed on to consumers through use of standard form contracts, and upon which suppliers have based their pricing to those consumers, can be eroded by the actions of a small section of consumers taking advantage of the unclear and untested provisions on a one-by-one basis. Sadly the costs of this would have to be passed on by traders to all consumers.
- 7.7 On the other hand, if the Ministry is concerned about contracts which may be unfair to consumers, it is strongly suggested that it would be preferable to encourage the use of contractual provisions (or documented internal policies) which are most likely to make a contract fair to consumers.
- 7.8 A statutory example is the cooling off period in the Credit Contracts and Consumer Finance Act which has its statutory requirement for transparency via the disclosure notices. A consumer is given the time to consider the contract terms and decide whether there is a better way. But having decided to continue in the contract, the consumer must then carry out his or her obligations: the trader is relying on the consumer's performance. Note that the effect of the Australian unfair contract terms provisions would render these "fair" terms irrelevant if another term fell within the grey list.
- 7.9 Other types of clauses which inherently create fairness in a consumer contract are:
- (a) Clauses which permit a consumer to assign a long-term contract;
 - (b) Clauses which provide for termination on hardship such as illness or redundancy;
 - (c) Clauses which permit a consumer to downgrade a long-term contract: either by opting in to a longer term and reducing

periodic payments or by choosing a shorter term and reducing total payments.

8. Conclusion

- 8.1 This submission does not support the inclusion of unfair contract terms provisions similar to those in the Australian Consumer Law in New Zealand law on the grounds that it is unnecessary, untested and creates costs which would be inevitably passed onto consumers.
- 8.2 On the other hand the submitter suggest that positive promotion of “fair” terms would be of benefit to consumers and to good traders.

Appendix

THE AUSTRALIAN CONSUMER LAW:

Part 2-3—Unfair contract terms

23 Unfair terms of consumer contracts

- (1) A term of a consumer contract is void if:
 - (a) the term is unfair; and
 - (b) the contract is a standard form contract.
- (2) The contract continues to bind the parties if it is capable of operating without the unfair term.
- (3) A **consumer contract** is a contract for:
 - (a) a supply of goods or services; or
 - (b) a sale or grant of an interest in land;to an individual whose acquisition of the goods, services or interest is wholly or predominantly for personal, domestic or household use or consumption.

24 Meaning of *unfair*

- (1) A term of a consumer contract is **unfair** if:
 - (a) it would cause a significant imbalance in the parties' rights and obligations arising under the contract; and
 - (b) it is not reasonably necessary in order to protect the legitimate interests of the party who would be advantaged by the term; and
 - (c) it would cause detriment (whether financial or otherwise) to a party if it were to be applied or relied on.
- (2) In determining whether a term of a consumer contract is unfair under subsection (1), a court may take into account such matters as it thinks relevant, but must take into account the following:
 - (a) the extent to which the term is transparent;
 - (b) the contract as a whole.
- (3) A term is **transparent** if the term is:
 - (a) expressed in reasonably plain language; and
 - (b) legible; and
 - (c) presented clearly; and
 - (d) readily available to any party affected by the term.
- (4) For the purposes of subsection (1)(b), a term of a consumer contract is presumed not to be reasonably necessary in order to protect the legitimate interests of the party who would be advantaged by the term, unless that party proves otherwise.

25 Examples of unfair terms

- (1) Without limiting section 24, the following are examples of the kinds of terms of a consumer contract that may be unfair:

- (a) a term that permits, or has the effect of permitting, one party (but not another party) to avoid or limit performance of the contract;
 - (b) a term that permits, or has the effect of permitting, one party (but not another party) to terminate the contract;
 - (c) a term that penalises, or has the effect of penalising, one party (but not another party) for a breach or termination of the contract;
 - (d) a term that permits, or has the effect of permitting, one party (but not another party) to vary the terms of the contract;
 - (e) a term that permits, or has the effect of permitting, one party (but not another party) to renew or not renew the contract;
 - (f) a term that permits, or has the effect of permitting, one party to vary the upfront price payable under the contract without the right of another party to terminate the contract;
 - (g) a term that permits, or has the effect of permitting, one party unilaterally to vary the characteristics of the goods or services to be supplied, or the interest in land to be sold or granted, under the contract;
 - (h) a term that permits, or has the effect of permitting, one party unilaterally to determine whether the contract has been breached or to interpret its meaning;
 - (i) a term that limits, or has the effect of limiting, one party's vicarious liability for its agents;
 - (j) a term that permits, or has the effect of permitting, one party to assign the contract to the detriment of another party without that other party's consent;
 - (k) a term that limits, or has the effect of limiting, one party's right to sue another party;
 - (l) a term that limits, or has the effect of limiting, the evidence one party can adduce in proceedings relating to the contract;
 - (m) a term that imposes, or has the effect of imposing, the evidential burden on one party in proceedings relating to the contract;
 - (n) a term of a kind, or a term that has an effect of a kind, prescribed by the regulations.
- (2) Before the Governor-General makes a regulation for the purposes of subsection (1)(n) prescribing a kind of term, or a kind of effect that a term has, the Minister must take into consideration:
- (a) the detriment that a term of that kind would cause to consumers; and
 - (b) the impact on business generally of prescribing that kind of term or effect; and
 - (c) the public interest.

26 Terms that define main subject matter of consumer contracts etc. are unaffected

- (1) Section 23 does not apply to a term of a consumer contract to the extent, but only to the extent, that the term:
- (a) defines the main subject matter of the contract; or
 - (b) sets the upfront price payable under the contract; or
 - (c) is a term required, or expressly permitted, by a law of the Commonwealth, a State or a Territory.
- (2) The *upfront price* payable under a consumer contract is 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.

27 Standard form contracts

- (1) If a party to a proceeding alleges that a contract is a standard form contract, it is presumed to be a standard form contract unless another party to the proceeding proves otherwise.
- (2) In determining whether a contract is a standard form contract, a court may take into account such matters as it thinks relevant, but must take into account the following:
 - (a) whether one of the parties has all or most of the bargaining power relating to the transaction;
 - (b) whether the contract was prepared by one party before any discussion relating to the transaction occurred between the parties;
 - (c) whether another party was, in effect, required either to accept or reject the terms of the contract (other than the terms referred to in section 26(1)) in the form in which they were presented;
 - (d) whether another party was given an effective opportunity to negotiate the terms of the contract that were not the terms referred to in section 26(1);
 - (e) whether the terms of the contract (other than the terms referred to in section 26(1)) take into account the specific characteristics of another party or the particular transaction;
 - (f) any other matter prescribed by the regulations.

28 Contracts to which this Part does not apply

- (1) This Part does not apply to:
 - (a) a contract of marine salvage or towage; or
 - (b) a charterparty of a ship; or
 - (c) a contract for the carriage of goods by ship.
- (2) Without limiting subsection (1)(c), the reference in that subsection to a contract for the carriage of goods by ship includes a reference to any contract covered by a sea carriage document within the meaning of the amended Hague Rules referred to in section 7(1) of the *Carriage of Goods by Sea Act 1991*.
- (3) This Part does not apply to a contract that is the constitution (within the meaning of section 9 of the *Corporations Act 2001*) of a company, managed investment scheme or other kind of body.