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Practice Group:

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Unfair Contract Terms with Small Businesses: Implications for the Construction Industry

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The unfair contract term prohibitions in the *Competition and Consumer Act 2010* (Cth) were recently extended to cover standard form contracts with small businesses.

The new law provides for unfair contract terms to be declared void and unenforceable. The relevant contract will then only continue to bind the parties insofar as it can operate without the unfair terms.

These changes may have significant impacts on the building and construction industry as terms typically found in construction contracts are likely to be subject to the prohibitions. We recommend that principals and contractors identify and review any standard form contracts they may have with small business counterparties that may be impacted by this new regime.

When will the prohibitions apply?

The law applies to a standard form contract entered into or varied on, or after, 12 November 2016 where:

- it is for the supply of goods or services, or the sale or grant of an interest in land
- one or more parties is a small business that employs fewer than 20 people
- the upfront price payable under the contract does not exceed AUD300,000 or, if the contract is for more than 12 months, AUD1 million.

These criteria are most likely to apply to subcontracts, supply agreements, plant hire agreements, consultancy agreements, minor works contracts and purchase orders involving small businesses.

A standard form contract is generally one which employs non-negotiated, standardised terms – that is, a contract offered on a "take it or leave it" basis, or one where there has been very little negotiation. When determining whether the contract is standard form, the Court will take into account any imbalance in bargaining power between the parties, the extent of pre-contract negotiations, whether the contract is tailored to the specific circumstances of the transaction and the characteristics of the counterparty. The prohibitions are likely to apply to template contracts offered by companies and may even extend to standard forms such as Australian Standards.

What is an unfair term?

A term will be unfair if:

- it would cause a significant imbalance of the parties' rights and obligations
- it is not reasonably necessary to protect the legitimate business interests of the party advantaged by the term
- it would cause detriment to the other party.

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Examples of terms that are likely to be considered unfair include terms that enable one party, but not the other, to have the benefit of broad indemnities, to limit or exclude liability, to unilaterally vary the contract, or to terminate the contract without cause.

Impacts for the construction industry

Until the Courts have handed down decisions under the legislation, there will be some uncertainty as to what will constitute an unfair term in a construction contract. However, conceptually an unfair term may include:

- unilateral variation clauses (especially when there is a requirement for the other party to comply with a variation before there is an agreement as to price and time)
- time bars to providing notices of potential claims such as claiming variations and extensions of time (especially those with short notice periods)
- termination for convenience clauses
- onerous warranties
- broad exclusion of liability clauses (i.e. "all care but no responsibility").

The practice of contractors passing through clauses from head contracts with principals to subcontractors is particularly relevant to the construction industry. In this situation, it will be important for a contractor to consider whether it has a legitimate business interest in including these types of terms in a contract with a small business. If there is an express pass-through obligation in the head contract, this may suffice as evidence of protecting a legitimate business interest.

What this means for you

If you have standard form contracts with small businesses that may be impacted by this new regime, it would be prudent to:

- carefully identify those businesses you deal with which fall within the definition of a small business for the purposes of the new law
- conduct a review of all existing standard form contracts with those identified small businesses that are current, or which you intend to utilise, and any existing contracts that are capable of renewal after 12 November 2016. Remember, that if a term in an existing contract is varied after 12 November 2016, it too will be subject to the protections provided by the new law.

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