

INQUIRY INTO UNFAIR TERMS IN CONSUMER CONTRACTS

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The Hon Christine Robertson
Chair, Standing Committee on Law and Justice
Parliament of NSW
Macquarie Street
Sydney NSW 2000

By email: lawandjustice@parliament.nsw.gov.au

Dear Ms Robertson,

Inquiry into unfair terms in consumer contracts

Consumer Credit Legal Centre (NSW) Inc and Redfern Legal Centre are pleased to provide a submission to the Law and Justice Committee's inquiry into unfair terms in consumer contracts.

Consumer Credit Legal Centre (NSW) Inc. (CCLC) is a specialist community legal centre. CCLC gives advice to consumers on credit and debt matters.

Redfern Legal Centre (RLC) is a generalist community legal centre. As part of the general matters that it advises on, RLC also has 2 solicitors who specialise in giving advice on credit and debt matters.

CCLC and RLC have had the benefit of reading the submissions from the Legal Aid Commission NSW, Consumer's Federation of Australia and CHOICE to this Inquiry. CCLC and RLC support the content of those submissions.

In particular, CCLC and RLC support the Recommendations listed in the CHOICE submission.

In summary

CCLC and RLC believe that there is an urgent need to introduce legislation prohibiting unfair terms in consumer contracts. We believe that this legislation is essential to protect consumers from unfair terms that arise in standard form contracts.

General Observations

This submission will start by making some general observations about the use of unfair terms in consumer contracts and then address the specific questions raised in the Terms of reference (TOR).

Unfortunately, it is our experience that with consumer contracts the only term that can be negotiated by a consumer is often the price. The standard form contract is not negotiable. As a consequence, the legal concept of a contract being a "meeting of minds" has no relevance to modern consumer contracts at all.

Consumers face the following problems when entering into a contract for consumer goods and services:

- The consumer cannot afford to obtain legal advice in relation to the contract. Even if the consumer did seek legal advice, the contract terms would not be negotiable anyway. The benefit of the legal advice would only be to ascertain whether the contract was so onerous as to be a poor decision.
- The consumer is unlikely to read the contract as the terms cannot be negotiated anyway. Furthermore, even if the consumer read the contract and found an unfair term it is probable that the same unfair term would be in a (similar) different supplier's contract.
- Consumers are so used to "one-sided non-negotiable contracts" that consumers have given up trying to negotiate "standard" terms.
- Consumers purchase lots of goods and services each year. It is completely impractical to negotiate and carefully consider each consumer contract.

Legislation prohibiting unfair terms is essential because:

- Consumers have no means to negotiate for the deletion of an unfair term from any standard contract
- Businesses will always seek to draft contracts as widely as possible to protect their own interests. The drafting of standard form contracts is for the most part completely unfettered by current consumer protection legislation. This is a poor outcome for consumers.
- The case law and legislation on unjustness and unconscionability is focussed on procedural unfairness. It is very rare for consumers to obtain a remedy for a substantively unfair term in a consumer contract.

- There has been a complete failure of competition to deliver fair "standard" terms in consumer contracts.

In summary, while consumer contracts are on a “take it or leave it” basis since businesses have similar terms, consumer protection legislation specifically prohibiting unfair terms is essential.

The Terms of Reference

(a) *Whether consumer contracts contain terms which cause a significant imbalance in the rights and obligations arising under the contract, to the detriment of the consumer?*

CCLC and RLC both contend that there are terms in consumer contracts which cause considerable detriment to the consumer.

i) terms which allow the supplier to unilaterally vary the price or characteristics of the goods or service without notice to the consumer;

Unilateral change clauses are extremely prevalent in all ongoing consumer contracts. The unilateral change clauses are drafted very widely to enable the supplier to unilaterally vary any aspect of the contract.

An example of a unilateral change clause appears in the RAMS home loan contract:

“We may vary any term of this agreement.”

Examples of the detriment causes by unilateral change clauses

EXAMPLE 1

Unilateral change of contract by Citibank

Citibank has recently been the subject of an investigation of its conduct by ASIC in relation to the use of its unilateral change clause for its Ready Credit credit card customers.

Citibank advertised a Ready Credit credit card with an interest rate of 4.99% p.a. There was an annual fee on the credit card. The credit card was very popular because of the low interest rate.

A great many consumers did not use the credit card at all for new purchases, but transferred their existing credit card balances to the Citibank credit card to take advantage of the low interest rate.

In response, Citibank used its unilateral change clause to introduce a new fee of \$160.00 which would be charged to any customer not using the credit card for new purchases.

ASIC investigated this matter and found there was no misleading conduct by Citibank. ASIC's press release on this issue dated 1/5/06 is available at www.fido.gov.au.

Although the conduct of Citibank was not misleading it was clearly unfair. Many, many consumers had applied for a Citibank credit card on the basis of the competitive interest rate. Some of those consumers would not have applied for the credit card if they had known a large fee (making the effective interest rate much higher) would be introduced if new purchases were not made on the credit card.

In effect, Citibank had used the unilateral change clause to vary the pricing of the contract so significantly that it was unrecognisable from the original contract the consumer had chosen to enter only a few months before.

EXAMPLE 2

Unilateral change of consent requirements

Ms. Z and Ms. A had a joint home loan with a well known mortgage originator. Mr. A decided to fix the interest rate on the loan without consulting or getting the consent of Ms. Z. The mortgage originator fixed the interest rate with the consent of only Mr. A. The home loan contract required that both parties must request that the interest rate be fixed.

When CCLC raised a dispute in relation to this matter, the mortgagor originator claimed that the requirement of joint consent had been unilaterally varied by it without notice.

ii) terms which penalise the consumer but not the supplier when there is a breach of the agreement;

Contracts drafted by suppliers never have any terms that provide for any penalty to the supplier for breach of the contract by the supplier.

Contracts drafted by suppliers include the charging of significant penalty fees and charges to consumers for the breach of the contract.

Examples of unfair penalties in consumer contracts

EXAMPLE 3

Late fees and overlimit fees on credit cards

It is now standard practice for lenders to charge fees for a late payment and/or overlimit use on a credit card. These fees can be as much as \$35 each month of default.

Penalty fees should be an estimate of the loss suffered by the supplier in the event of the consumer defaulting on the contract. Any fees or interest charged in excess of the genuine pre-estimate of loss is a penalty which is not owed by the consumer.

In the UK, the Office of Fair Trading has recently reviewed the charging of these fees in the context of its unfair terms legislation.

The review found in many cases the fees were excessive and in the case of overlimit fees this fee could not be reasonably charged at all.

This means that in the UK, consumers have protection from excessive penalty fees and unfair fees, however, in Australia consumers are still being charged unfair and excessive fees.

EXAMPLE 4

Penalty fees in loans

CCLC had a case recently where a consumer had fallen into default with her loan due to illness. The loan contract provided that each time the bank sent an arrears notice the consumer would be charged \$45.

The bank proceeded to send many arrears notices and charged the consumer \$45 each time a notice was sent. Over a few months the bank had managed to charge the consumer almost \$1000 in arrears notice fees.

It is our contention that the fee being charged did not represent the true cost of sending the letter and the repetitive sending of notices (and charging a fee each time) was unfair in the circumstances.

EXAMPLE 5

Photographic contracts

RLC and other legal centres have dealt with a number of cases in which a

particular company tells young women that they have “won” a free make-up and photo-shoot session, but then hassles them into paying up to \$3,000 for a “package” of photos which might include only a few of the photos that the woman actually wants. *These cases involve not only procedural injustice, but also substantive injustice.*

The contracts to which the company signs up the young women are full of unfair terms. For example, the contracts state that the company can give personal information about the client, to a credit reporting agency.

*“Personal information” is defined to “include” certain items, but is not exhaustive, and hence could also include other, non-specified items such as the woman's criminal record. One of the items which **are** specified is if the young woman has, “in the opinion of the company, committed a serious credit infringement “.*

If the client defaults in any way, then:

- the whole purchase price becomes payable. The whole purchase price is defined as being the price before any discounts offered for early or “prompt” payment of the account;
- an “account service fee “of \$25” per transaction (whether by mail or personal phone call” is added to the account; *and*
- the client is liable to pay all costs, charges and expenses reasonably incurred by the use of solicitors or any other method of collection.

If some or part of the payment is overdue, the company may take back the photos and sell them, and may “enter upon the client’s premises ... for that purpose”. *This extraordinary provision purports to give the company powers which even police do not normally have (except in cases such as suspicion of criminal activities).*

The company is not liable for non-delivery or delay caused by “plant or equipment breakdowns, ... accidents, or any cause whatsoever”.

The client cannot “reply (sic) upon any other condition ... or representation whether oral or in writing as adding to or amending or negatives (sic) terms ... or representations as set out in these conditions of sale”. *This seems to be an attempt to negate well-established principles of both common law and statute law relating to the construction of contracts (e.g. see Cheshire and Fifoot, “Law of Contract”, chapter 4).*

The company “is not subject to any condition ... or liability in respect to (sic) the

condition merchantability or fitness for purpose of any goods sold to the client ... except for any ... liability which is implied or imposed herein or by virtue of any applicable statute in which case [the company's] liability shall be limited to the replacement of the goods ... as determined by [the company] in its absolute discretion”.

Some of the clauses set out above are not merely unfair (e.g. by being unbalanced in favour of the company) but also probably illegal under *various statutes, both Federal and State*.

In addition to the contract described above, clients *of this particular company* are required to sign a statement that the copyright in the photographs remains the property of the company. There is a preliminary question as to whether separate copyright exists in, say, the actual photo on the one hand, and the image, on the other. As far as unfair terms in contracts are concerned, however, it is extraordinary for a person to pay a company to take over ownership of the person's copyright, rather than the other way round. Usually you sell your own copyright in an artistic item; you don't pay others to take it away.

EXAMPLE 6

Car Hire Contracts

One car rental company which targets backpackers floated a contract a couple of years ago which, amongst other clauses, contained the following:

“the renter of the vehicle is liable to the owner for any damage caused if ‘the renter has without consent in writing of the owner made given (sic) any offer, promise of payment’ [etc] “in respect of any damage to the vehicle or the property of any third person”.

Another clause said that the renter will be responsible “for overhead damage to the vehicle caused by its (sic) failure to clear low trees, bridges or other objects”.

EXAMPLE 7

Mobile phone contracts

In the early years of the spread of mobile phones, many young people contacted us about problems they were having with mobile phone debts. A study by Dr. M. Griffiths of the University of Newcastle found that 34 per cent of young people (18-24 years old) had telephone debts, with 78 per cent of these owed to mobile phone companies. (SMH November 22-23, 2003.)

In the course of investigating these cases, we discovered that mobile phone contracts contained a myriad unfair terms.

The kinds of unfair terms in the contracts included:

- the ubiquitous unilateral change clauses (which of course enabled the telco carrier or the supplier of the handset, but not the consumer, to change the terms of the contract);
- penalty clauses – which enable the carrier or provider to impose a penalty on the consumer if s/he fails to pay, say, one instalment on time. This often means that a consumer could miss one payment and the whole contract becomes payable and they do not even get to use the phone for the remainder of the contract;
- terms which limit the liability of suppliers; and
- terms which enable the service provider to pay commissions to dealers or retailers, without specifying how much those commissions are or for what period of time they can be paid.

Pre-paid mobile phone cards seem to have reduced the number of young people contacting us with mobile phone debts, but we are not sure that this necessarily means that phone contracts have improved.

EXAMPLE 8

The mystery of the missing phone contracts.

It was commonplace for telcos, *when contacted by us*, to say that they had lost or mislaid the contract actually signed by our client. They were always able to provide us with a pro forma version, however. We would then argue that without the actual contract, how could it be established whether or not the terms had in fact been subject to negotiation between the parties, and hence, what in fact had been agreed upon? In all such cases, the telco would ultimately agree to waive our clients' alleged debts.

In one missing contract case, we filed a Notice of Motion seeking to have a default judgment set aside by the Court on the ground that there was no evidence that our client had signed the contract in question. The telco involved did not even bother to put on a defence. Rather, it agreed to waive our client's alleged debt. Similarly, another mobile phone company had sued our client for a debt, but for some reason had not been able to provide us with a copy of the contract signed by our client. The case went as far as the solicitors for each party turning up at the hearing and commencing argument. When the RLC solicitor raised in court the issue of the mystery of the vanished contract, the solicitor for the telco promptly discontinued its action against our client and offered to pay our client's

costs.

Perhaps lack of written evidence of what had been agreed upon by the parties was not what the telcos were worried about. Perhaps they were more concerned about having their contracts put before a court at all.

On at least one occasion it became problematic for the telco when it *did* provide us with a copy of the contract allegedly signed by our client. The client's copy said that there was an early disconnection fee "as listed above, or \$450 if not listed". Our client's copy of the contract had no fee "listed above". The copy provided by the telco had a fee of either \$50 or \$60 written in this space – it was hard to tell which, because the writing was so bad. An employee of the debt collection company (to which the telco had either sold or passed the debt) tried to tell our solicitor that a \$450 disconnection fee applied to our client's contract.

In addition in this case, the telco had unilaterally increased our client's "monthly access fee" from \$15.00 to \$30.00 in breach of its own contract term which said that the terms of the contract could be varied "only by the agreement of both [X company] and the customer in writing".

If the inclusion of certain types of contract terms is unfair, the *lack* of certain terms can also be unfair. For example, it is unfair if there is no provision for notice to be given to a consumer before punitive action is taken by the provider of the good or service. This principle is recognised by the Uniform Consumer Credit Code in its notice provisions.

EXAMPLE 9

Consumer leases

A number of major consumer lease companies have a term in their contract that states that if the consumer defaults on the lease then the entire amount to be paid during the entire term of the lease is owed by the consumer as liquidated damages.

This is an excessive penalty. It is particularly harsh when the consumer does not even get to continue to lease the goods yet has to pay the lease as if they had leased the goods.

EXAMPLE 10

Vendor Finance

Vendor finance is when a consumer buys a home from the vendor by paying regular instalments over a number of years. The vendor usually has a loan for the property and the instalment contract provides that the purchaser pays that loan plus an additional margin of interest. This is the way the vendor makes a profit.

Vendor finance contracts almost always contain a term that states:

“ the Purchaser shall forfeit to the Vendor and the Vendor shall keep the deposit and all instalments paid under this Contract, as liquidated damages for non-performance of the Contract, without necessity for the Vendor to give notice or to do any other thing; and the Purchaser shall retain no title to the improvements to the property and replacement to fixture (all of which all remain with the property) and the Purchaser shall have no claim against the Vendor for the cost or value of any improvements or replacement to fixtures made by the Purchaser to the property.”

This means that the Vendor retains all the instalments and the deposit (which is usually the first home buyer’s grant) in the event of default by the purchaser. This is an extremely unfair term.

This term has recently been considered in a case in the Consumer Trader & Tenancy Tribunal in NSW being *Lewis v. Ormes* (2005) NSWCTTT 481 (18 July 2005). The decision in this case was confirmed on appeal in the Supreme Court.

The CTTT found that the above term was unfair.

However, as there is no unfair terms legislation in NSW this now means that every consumer affected by the unfair term will need to pursue the matter through the CTTT for justice.

This is an extremely inefficient way to deal with a standard unfair term. It ties up the resources of the CTTT and the Court system. It is also extremely unfair that there are almost definitely a number of affected consumers who are not even aware of the fact that this term has been found to be unfair.

However, the most awful consequence is that the unfair term continues to be used by vendor financiers all over Australia.

iii) terms which allow a supplier to suspend services supplied under the contract while continuing to charge the consumer; or

See above examples under consumer leases and mobile phone contracts.

iv) terms which permit the supplier but not the consumer to terminate the contract.

Consumer leases and mobile phone contracts permit the supplier to terminate the contract at any time but not the consumer.

(b) *The remedies available under common law and statute with respect to unfair terms in consumer contracts.*

The current remedies for unconscionability (common law, Trade Practices Act, State and Territory Fair Trading legislation), unjust contracts (Contracts Review Act NSW), and unjust credit contracts (Uniform Consumer Credit Code) are inadequate for the following reasons:

- Consumer access to justice is limited. So even if a consumer has a case concerning an unfair term it is very expensive to use a solicitor.
- The Courts have very rarely found that there has been procedural unfairness
- Unjustness and unconscionability are circumstances based. This means that even if there are common unfair terms in cases this still will not provide a useful precedent.
- It is inefficient to deal with “standard form” unfair terms on a case by case basis
- Unjustness is focussed on a lack of benefit to the consumer. The Courts have failed to develop a body of precedent law that focuses on unfairness for its own sake.

(c) *The effectiveness of specific purposes legislation, such as the UK Unfair Terms in Consumer Contracts Regulations 1999 and the Victorian Fair Trading Act 1999 (Part 2B – Unfair Terms in Consumer Contracts)*

Specific purpose legislation is essential as the general legal remedies relating to unjustness have failed to provide any remedy for consumers in relation to unfair terms.

Specific purposes legislation is required to take preventative action in relation to unfair terms. Unfair terms can be identified by the regulator and removed across many standard contracts in a whole range of consumer contracts.

Consumers would then have some confidence that the contracts they sign have been reviewed with any unfair terms removed.

(d) *Any other relevant matter*

It is highly preferable that any unfair terms legislation be national. However, in the absence of the preferred national approach introducing legislation in NSW to protect consumers from unfair terms is urgently required.

Yours sincerely

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