



**Submission to the
Productivity Commission**

on

**Unfair Contract Terms in Consumer Contracts arising from the
publication of its Draft Report on**

Review of Australia's Consumer Policy Framework

December 2007

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building australia



1.0 INTRODUCTION

- 1.1 This submission is made by Master Builders Australia Inc (Master Builders).
- 1.2 Master Builders represents the interest of all sectors of the building and construction industry. The association consists of nine State and Territory builders' associations with over 30,000 members.
- 1.3 Jointly with The Royal Australian Institute of Architects (RAIA), Master Builders prepares standard form contracts for sale. These contracts form the Australian Building Industry Contract (ABIC) Suite. The ABIC suite of contracts is a new generation of standard form, plain English building contracts for use in all market sectors, domestic and commercial, which were first published in 2001, refined and added to in 2002 and updated and republished in 2003. Throughout 2006 and 2007 further changes have been made for release of a new version of the contracts and these will be marketed early in 2008. As stated, ABIC contracts are used in all building and construction industry markets, commercial, domestic and civil.
- 1.4 ABIC is the latest in a range of joint building industry contracts with which Master Builders has been associated, as has the RAIA. These contracts do not contain any bias for or against consumers. Master Builders is well placed, therefore, to provide comment on issues surrounding the nature and incidence of allegedly unfair contract terms in standard form contracts, a matter raised with Commission personnel during meetings on the current reference. This is an issue which is of great concern to Master Builders and, accordingly, this submission is addressed to the findings of and the recommendations that emanate from Chapter 7 of the Draft Report entitled *Review of Australia's Consumer Policy Framework*.
- 1.5 A submission on the issues raised in Chapter 7 is also useful in the context of the election of the new government. In the lead up to the election, the Australian Labor Party stated that it wanted amendments to the *Trade Practices Act* which were then before the Commonwealth Parliament to be "strengthened." In particular it wanted the then Government to "closely examine options for introducing an 'unfair

contract terms' regime based on the UK and Victorian models."¹ In our estimation Chapter 7, and the comprehensive Appendix D to the Draft Report, stand as an appropriate analysis of the options for introducing such a regime and we have therefore provided a copy of this submission to The Hon Chris Bowen MP, Assistant Treasurer and Minister for Competition Policy and Consumers Affairs; The Hon Dr Craig Emerson MP, Minister for Small Business, Independent Contractors and the Service Economy; and The Hon Lindsay Tanner MP, Minister for Finance and Deregulation.

- 1.6 Master Builders commends the main focus of the report that is upon individuals making purchases of goods or services for private use. Master Builders supports this perspective, and opposes any unfair contracts proposals being extended to business to business contracts.
- 1.7 Other aspects of the Draft Report will be considered in separate communications.

2.0 PURPOSE OF THIS SUBMISSION

- 2.1 Unfair contract terms may be broadly defined as those terms in a contract which are to the disadvantage of one party (usually the purchaser of goods or services) but which are not reasonably necessary for the protection of the legitimate interests of the other party (usually the supplier). The Commission has recognised this in the Draft Report. Building and construction industry standard form contracts, in particular, are often wrongly labelled as having a "non-negotiated character." This submission outlines the Master Builders' response to draft recommendation 7.1 dealing with the issue of unfair contracts which embraces this definition. For convenience a copy of the draft recommendation is attached as Attachment A.

¹ Media statement by Mr Chris Bowen and Dr Craig Emerson *Labor Moves to Strengthen the Trade Practices Act* 7 August 2007 <http://www.alp.org.au/media/0807/msatsbic070.php> accessed 13 December 2007

- 2.2 In the building and construction industry even the “standard” printed conditions can be – and routinely are – altered, added to or deleted. None of the major terms of building contracts such as price, quality, length of contract time, security for performance, insurances, dispute resolution methods, liquidated damages etc are “standard”, but are required to be individually negotiated and inserted into each contract.
- 2.3 Master Builders’ experience is that special conditions are frequently added to the ABIC and Master Builders pro forma contract documents. We note that the ABIC contracts permit that to occur within their structure. At the outset, we reject any notion that a standard form contract necessarily indicates a lack of good faith on the part of its proponent. Similarly, we do not agree that there is no distinction between a lack of good faith and per se unfairness, a matter that needs more exploration in the Draft Report.
- 2.4 Master Builders principal contention is that there should be no additional regulation along the lines of Part 2B *Fair Trading Act, 1999 (Vic)* and we support modification of that model, if the Commission’s recommendations are to be taken up by Government. Constraints on economic freedoms should be closely scrutinised and be the subject of proper regulatory impact statements. As noted by the Commission, the negative implications for all consumers by the imposition of higher costs for an amorphously defined benefit mean that the ambit of any new law should be closely confined: see discussion of this point in particular at last paragraph on page 122 of the Draft Report. In the simplest terms, a bargain that can be undone after it is struck must unavoidably be priced higher at the outset, if an industry sector is to be sustainable.
- 2.5 If there is to be regulation to protect non-business consumers, Master Builders believes that there should be a sector by sector approach, not one size fits all regulation. This latter point is especially the case given the consumer protection orientation of current domestic building legislation throughout Australia (see box) and the generally rigorous protection afforded to building industry consumers by that legislation, albeit in a highly non-uniform manner.

Domestic Building Contracts Acts

Name of Act/Statute/Regulation	State/Territory
<i>Building Act 2004</i> Building Amendment Regulations 2004	Australian Capital Territory
<i>Home Building Act 1989</i> Home Building Regulation 2004	New South Wales
<i>Building Act 1993</i> Building Regulations	Northern Territory
<i>Domestic Building Contracts Act 2000</i> Domestic Building Contracts Regulation 2000	Queensland
<i>Building Work Contractors Act 1995</i> Building Work Contractors Regulations 1996	South Australia
<i>Building Act 2000</i> Building Regulations 2004	Tasmania
<i>Domestic Building Contracts Act 1995</i> Domestic Building Contracts Regulations 2007 <i>Building Act 1993</i>	Victoria
<i>Home Building Contracts Act 1991</i> Home Building Contracts Regulations 1992	Western Australia

2.6 Master Builders is strongly of the view that any new legislation not become a costly overlay on the existing law. This has occurred in Victoria. Under the Victorian model for domestic building legislation, and followed in several other jurisdictions, consumers are urged to read the contract and there are built in protections for consumers including cooling off periods. Further, under the Victorian Act, it is a pre-condition to the entering of a valid contract that:

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| <ul style="list-style-type: none"> • the builder supplies the owners with a draft contract; and • the owners familiarise themselves with the contract – including the seeking of advice if necessary; and • the owners complete a questionnaire bound into the contract; and • they can and do truthfully answer “yes” to each question. |
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The relevant questionnaire also contains a mandatory warning that the owner is not ready to sign the contract if he or she cannot truthfully answer yes to all questions. A cooling-off period is additional to these provisions. There exists a raft of protections that Master Builders contends do not require the additional application of an unfair contracts jurisdiction. The legislation also invokes mandatory contract provisions, such as that there must be agreement in writing by the consumer to variation of the contract, plans or specifications, and codifies common law warranties as incorporated into the contract.

2.7 In New South Wales and Victoria the legislation invokes mandatory contract provisions that must be contained in residential building contracts. As well as a mandatory cooling off period of five (5) days, foundational consumer protection provisions include:

- all plans and specifications for work to be done under the contract including variations form part of the contract by operation of law;
- any agreement to vary the contract, plans or specifications must be in writing and signed by each party; and
- all work under the building contract must comply with the Building Code of Australia and all other relevant codes, standards and specifications that the work is required to comply with under any law.
- Section 18B of the NSW Act incorporates mandatory warranties into every contract within jurisdiction.

- 2.8 In addition, a compulsory questionnaire has been incorporated into all NSW domestic building contracts. There are a series of questions posed which prompt the party entering into the contract to consider various procedural and job specific matters for their protection. Questions range from recognising whether or not the builder has a licence to cover the work under the contract to an acknowledgement by the consumer that certain provisions may change the price. Consumers are also notified about the requirement for home warranty insurance to be effected by a builder where the cost of the works exceeds \$12,000 and there is a requirement that consumers receive a booklet prepared by the Office of Fair Trading, Department of Commerce New South Wales setting out advice in an approved form.
- 2.9 Section 89D *Home Building Act 1989 (NSW)* relating to jurisdiction concerning unjust contracts provides to the relevant Tribunal, the Consumer Trader and Tenancy Tribunal, the jurisdiction of the Supreme Court under the *Contracts Review Act 1980 (NSW)* with regard to contracts for residential building work, building consultancy work, or specialist work. The only restriction on the power available to the Tribunal under the Act is a prohibition from exercising power under s.10 *Contracts Review Act 1980*.² In effect, NSW has an unfair contracts jurisdiction in place at the moment.
- 2.10 It is clear therefore that in Victoria and in NSW a large number of consumer protections are in place, with many such protections echoed in other states and territories. Master Builders' strongly contends that there is no need to add to the existing body of regulation that provides more than adequate protection. Most building contracts are executed following prolonged negotiations and the transparency of the obligations that the consumer is to become bound to should be palpable under the current legislative models. The cooling off period then permits a final opportunity for the consumer to decide to cancel

² Section 10 is as follows: Where the Supreme Court is satisfied, on the application of the Minister or the Attorney General, or both, that a person has embarked, or is likely to embark, on a course of conduct leading to the formation of unjust contracts, it may, by order, prescribe or otherwise restrict, the terms upon which that person may enter into contracts of a specified class.

the contract without adverse commercial repercussions, an opportunity the builder does not get. This obligation flows only one way and therefore sophisticated consumers may take advantage of builders; if the builder, for example, makes an omission in estimating its costs, no cooling off period is available to relieve that burden.

2.11 The Queensland legislation in turn has a comprehensive system of regulation where, for all domestic work over \$3,300, there are specific requirements for contractual terms dealing with:

- Contracts to be in writing
- Cooling off period of five (5) days
- Contract Information Statement
- Warning notice that contract price can change and under what provision
- Foundation Data
- Deposits and the limitations
- Construction period and how it is calculated and administered
- Variations on how it is priced, agreed and administered
- Progress payments
- Cost escalation not Rise and fall
- PC and provision sums

2.12 In the context just discussed, we agree with the Commission's comment on page 124 that specific attention is required of regulators in this area so that consistency of enforcement is provided and jurisdictional overlaps do not occur. In regard to the regulation of domestic building work, there is already a highly inefficient regulatory overlap that should not be compounded by new consumer protection law that would only act as an unnecessary overlay to the existing protections, adding to complexity.

3.0 THE ISSUE WITH THE VICTORIAN LEGISLATION

- 3.1 Introduction of the Victorian unfair contract provisions model will compound the confusion elsewhere. The gist of the problem of confusion in Victoria, as in other states and territories, in addition to the protections outlined above, is that a readily accessible Tribunal already has the power under the building legislation to negate the effect of any builder/consumer contract on the ground of unfairness. Application to the Tribunal requires no lawyer and a minimal fee. Further, both Consumer Affairs Victoria and the State Building Commission provide extensive information, advice, advocacy and dispute resolution services at nominal or no cost to consumers of domestic building work. These services include conciliation, the commissioning and obtaining of independent expert reports, litigation and prosecution on behalf of consumers and disciplinary actions against registered building practitioners. Application of new legislation to an already over-regulated industry sector is contradictory and simply not justified. An overlay of the new unfair contracts provisions is both unnecessary, a duplication, and potentially disastrous if it is able to interpret contractual “fairness” with the benefit of hindsight.
- 3.2 Master Builders is of the view that the idea of focussing upon categorisation of terms as inherently unfair is fundamentally at odds with the history of the development of contract law and will not advance competition or the certainty necessary to found business planning. The notion of when, as is currently legislated in the *Fair Trading Act* of Victoria, a contract “causes a significant imbalance in the parties’ rights and obligations under the contract, to the detriment of the consumer” is extraordinarily subjective, especially as this criterion covers issues of price, a matter touched upon on page 123 of the Draft Report. When does a consumer pay too much and why should the law transfer the risk of the consumer paying, say, more than a market price at a fixed instant in time to a supplier? Is the answer to these questions a matter that should be regulated via the courts with the benefit of hindsight in different economic circumstances to those when the contract is formed? We think not.

3.3 We note that, as pointed out on page 123 of the Draft Report, the UK regulations do not cover price setting so long as those provisions are in plain, intelligible language. We have urged the Victorian government to so change the legislation in that State. Manipulation of price by any external agency that interferes with this potent signal in the market economy³ should be the subject of thorough study for its effect on each market that is sought to be regulated; on this basis, we note with approval the criterion identified by the Commission that the application of any law should explicitly exclude terms dealing with ('non-contingent' or upfront) standard contract prices in order to preclude risks of inefficient price regulation. We emphasise that this approach was not adopted in the Victorian legislation. This is a particularly significant point where, as in the building and construction industry, price is not commodity-based but relates to value and quality. A single "fair" price assumes uniform quality and uniform service or product standard.

4.0 THE PRIMARY RESPONSE

4.1 Master Builders believes that any identified problem is not causing sufficient detriment in the residential building market place to justify further intervention. As indicated by the Commission, further regulations will be priced into transactions by the industry resulting in higher prices without a necessary commensurate increase in consumer protection. If there are difficulties in other particular sectors, such as in the car rental market with contracts of adhesion, then sectoral specific legislation should be investigated once the relevant problems have been sufficiently identified. This identification process should include consultation with the industry sector to be regulated and should include a comprehensive study of the problem in economic terms through a Regulatory Impact Statement, given the magnitude of the intervention in the marketplace. The Commission traverses this option, referring it as regulation of "hot spots" at page 125 to 126 of the Draft Report.

³ As Friedman notes:

"Prices perform three functions in organizing economic activity: first, they transmit information; second, they provide an incentive to adopt those methods of production that are least costly and thereby use available resources for the most highly valued purposes; third, they determine who gets how much of the product – the distribution of income." M Friedman, R Friedman "Free to Choose" 1980, p.33.

- 4.2 The option is dismissed by the Commission largely on the basis that it would be difficult to assess “where the hotspot list would stop.” This question is easy to answer where the process would be exclusionary, ie the regulatory authority had identified that there was already sufficient regulation of the particular subject or industry to exclude the unfair contracts jurisdiction. Master Builders contends that by using a more appropriate test the already over-regulated area of domestic building contracts should be excluded and hence this “exclusionary” process should be considered by the Commission.

5.0 DOMESTIC BUILDING LEGISLATION

- 5.1 The current law recognises that some consumers may be vulnerable. It recognises that suppliers may have a superior bargaining position to consumers. The law has more than overcome the problem of a supplier taking advantage of a domestic consumer through a superior bargaining position. It has swung the pendulum in favour of consumers, even where the consumer has greater marketplace power than, say, a small builder. Generally, the statutes protecting consumers in the building and construction industry fulfil this function by ensuring they have sufficient information about the contract in a readily accessible form and that they have an opportunity to “cool off” after entering into the contract. With a purchase or transaction of such significance, a further consumer protection may be a requirement to seek independent advice prior to signing any contract. This would certainly be a more efficient measure than the form of regulation currently in place in Victoria and would assist consumers to a greater extent that if a new jurisdiction was erected, as proposed by the Commission.
- 5.2 On the basis of the force of the laws protecting domestic building consumers, we advocate no further changes to effect greater levels of protection. Instead, we advocate reform along the lines implied by the following statement from the Productivity Commission’s research report entitled *Reform of Building Regulation*:⁴

Clear and consistent minimum requirements for home building contracts could go some way to addressing potential

⁴ 17 November 2004 <http://www.pc.gov.au/> accessed 13 December 2007

*information asymmetries between consumers and builders in this section of the market. This, together with general information provided with contracts outlining processes and the parties' rights and responsibilities, would help in clarifying consumers' expectations and identifying the risks that they are assuming.*⁵

- 5.3 The relevant research report, however, did not go on to recommend that national harmonisation of domestic building contractual requirements should occur, noting that net benefits might not be generated given the extent of the current diversity in regulatory regimes, a finding that prima facie appears circular. Master Builders suggests expansion of this argument and exploration of the exclusion of the domestic building area from the Commission's current draft recommendation shown as Attachment A to this submission.

6.0 CONCLUSION

- 6.1 Master Builders recommends that the Productivity Commission specifically exclude the domestic building industry from any proposed unfair contract laws on the basis that sufficient consumer protection currently exists.
- 6.2 In the alternative, Master Builders advocates that the model proposed by the Commission be applied by way of inter-governmental agreement, including in Victoria, and that the Victorian model be rejected for the reasons set out in the Draft Report and referred to in this submission. Indeed there are positive features to the Commission's recommended federal scheme as follows:
- The definition of "unfair" includes unfairness to both sides;
 - It introduces a threshold criterion of material consumer detriment and insists on evidence of this;
 - The upfront contract price is not subject to examination;
 - It requires demonstration of an overall public benefit from any proposed remedial action;
 - It would encompass the establishment of "safe harbour" terms
 - The right to determine that –

⁵ Id at p 229

- A breach has occurred; and
- What, if any, restraint should be applied to a proven offender's activities

is reserved to the Courts (and not delegated to civil servants or given to tribunals).

6.3 Master Builders would be pleased to expand upon this submission in any public hearings on the Draft Report.

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Chapter 7 — Unfair contracts

DRAFT RECOMMENDATION 7.1

A new provision should be incorporated in the new national generic consumer law that voids unfair terms in standard form contracts, where:

- *the term is established as ‘unfair’: that is, it is contrary to the requirements of good faith and causes a significant imbalance in the parties’ rights and obligations arising under the contract;*
- *there is evidence of material detriment to consumers;*
- *it does not relate to the upfront price of the good or service;*
- *all of the circumstances of the contract have been considered; and*
- *there is an overall public benefit from remedial action.*

Where these criteria are met, the unfair term would be voided only for the contracts of those consumers subject to detriment, with suppliers also potentially liable to damages for that detriment.

There should also be a capacity for an industry or business to secure regulatory approval for ‘safe harbour’ contract terms that would be immune from any action under this provision.

The operation and effects of the new provision should be reviewed within five years of its introduction.

[extract from Review of Australia’s Consumer Policy Framework - Productivity Commission, Draft Report Recommendations of 12 December 2007]