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Law

New Directions in How Legislators, Courts, and Legal Practitioners Approach Unconscionable Conduct and Good Faith

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Topical Litigation and Possibilities

- class actions on bank fees (eg *Andrews v ANZ*)
- margin calls on share portfolios (eg *Goodridge v Macquarie*)
- Storm litigation and regulatory action
- targeting financially inexperienced investors with exploitative share purchase offers (eg *ASIC v National Exchange*)
- advantage-taking of financially distressed borrowers by mortgage brokers
- 'low doc'/'no doc' loans, asset lending, and brokering to avoid consumer protections
- calling up bank guarantees
- recalibrating pre-GFC and post-GFC concessions/conditions for credit
- companies as victims of unconscionable conduct (eg exploiting financially stressed companies with 'tied hands')
- creating illusory bidding war in competitive takeover/bidding processes

What's New or Different in UC Regulation?

- Unclear scope of statutory and non-statutory UC after decades of litigation and legislation
- Parliamentary + Expert Panel Reports 2008-2010
- ACL and 'unfair contract terms' regime 2010-2011
- Addition to listed indicators of statutory UC
- New regulatory powers apply to UC (eg pecuniary penalties and infringement notices)
- New principles of interpretation for statutory UC from 2012
- Harmonisation of B2C and B2B unconscionability from 2012
- Meaning of GF as indicator of statutory UC?

What's New or Different in GF Regulation?

- Current judicial/academic debate - implied terms or 'implicit good faith'?
- Honesty + contractual cooperation/fidelity + non-arbitrary/capricious + reasonableness? – and what kind of 'reasonableness'?
- Overlap/interaction with cognate implied obligations (eg cooperation, non-frustration etc)
- All/most commercial contracts and tests for implication?
- Limits of exclusion through drafting?
- Transactional perspective – GF in contract + GF in statutory UC:
 - Limits on private agreement?
 - Impact on content of good faith?
 - Advice: cover both aspects where needed?
 - Pleading: plead GF deficiency in contract and statutory UC?
- More nuanced client options and drafting techniques:
 - Not as simple as adopt/exclude
 - Combination of clauses needed
 - Different expectations for different clients/industries

‘Hot’ Industry Areas for UC/GF Regulation

- Loan and security arrangements
- Financial services and advice
- Share dealings and investments
- Franchising
- Commercial leasing
- Building and construction
- Telecommunications
- Termination/default contexts (all areas)
- ACCC Chairman Rod Sims (Feb 2012): ‘Unconscionable conduct between businesses is another area of attention this year and one of particular concern to small business ... Proving UC is, of course, a high hurdle, but where it occurs the ACCC will not hesitate in taking action.’

HCA Precedential Directive – *Farah Constructions v Say-Dee*

- ‘Intermediate appellate courts and trial judges in Australia should not depart from decisions in intermediate appellate courts in another jurisdiction on the interpretation of Commonwealth legislation or uniform national legislation unless they are convinced that the interpretation is plainly wrong. Since there is a common law of Australia rather than of each Australian jurisdiction, the same principle applies in relation to non-statutory law.’
- ‘Generally speaking, recent decisions at first instance and by intermediate courts of appeal (particularly the NSWCA) have recognised that an obligation of good faith in the performance and execution of contractual obligations and powers “may be implied as a matter of law as a legal incident of a commercial contract”. Alternatively, other decisions at first instance, and by the Victorian Court of Appeal, have approached the issue as one of implication of fact.’ (CJ Marilyn Warren, Supreme Court of Victoria)

Unconscionable Conduct Relates to ...

- Various equitable causes of action and bases for relief
- Statutory unconscionability under Competition and Consumer Act
- Statutory unconscionability in financial services under ASIC Act
- Unconscionable financial services licensee conduct under Corporations Act (s991A)
- Unjust contracts laws (eg NSW Contracts Review Act)
- Industry codes (eg Banking/Franchising Codes)
- State retail/commercial leasing laws

Three Basic Forms of Statutory Unconscionability

- **General prohibition - unconscionable conduct:**

- Old TPA s 51AA (in trade practices generally)
- New CCA ACL, section 20
- ASICA s 12CA (in financial services)
- Corporations Act s 991A (financial services licensees)

- **Unconscionable conduct in retail/personal/consumer contexts (ie B2C unconscionability):**

- Old TPA s 51AB
- New CCA ACL, sections 21 and 22
- ASICA sections 12CB and 12CC

- **Unconscionable conduct in big/small business contexts (ie B2B unconscionability):**

- Old TPA s 51AC
- New CCA ACL, sections 21 and 22
- ASICA sections 12CB and 12CC
- Some state commercial/retail leasing Acts

Competition and Consumer Act 2010 (Cth) (*As of 6 June 2012*)

20 Unconscionable conduct within the meaning of the unwritten law

(1) A person must not, in trade or commerce, engage in conduct that is **unconscionable, within the meaning of the unwritten law** from time to time.

Strands of Unconscionable Dealing

- **GARCIA-Type UC**
 - Wife (or other close relationship?)
 - Guarantees husband's personal/business debts
 - Failure to understand
 - A volunteer (no benefit)
 - No or inadequate explanation
 - Relevant factors known to bank
 - Bank remedial actions inadequate
- **AMADIO-Type UC**
 - Weaker party under a special disadvantage
 - Special disadvantage can be personal (eg illiteracy)
 - Special disadvantage can also be financial, legal, or informational (ie 'situational')
 - Disadvantage affects weaker party's capacity to decide best interests
 - Stronger party knows and takes advantage of that disadvantage
 - Exploitation of that disadvantage in the circumstances is against 'good conscience' in legal terms

Meanings & Levels of Unconscionability Regulation

Under ‘the Unwritten Law’ (4 categories as described by Paul Finn):

- [1] Unconscionability as the underlying concept for Equity as a whole
- [2] Unconscionability as an element or finding that is essential for specific equitable actions (eg estoppel, relief against forfeiture, unconscionable dealings, unilateral mistake etc)
 - Coercion/exploitation/advantage-taking
 - Unconscionable exercise of rights, retention of benefits etc
- [3] Doctrines & remedies associated with unconscionable dealings & exploitation, advantage-taking, and defective understanding:
 - ‘spousal guarantees’ rules (eg *Yerkey v Jones, Garcia*)
 - ‘special disadvantage’ rule (eg *Amadio/Berbatis*)
 - Others (eg *Bridgewater v Leahy*)
- [4] Unconscionability as a direct ground of relief in its own right, unmediated by conventional doctrines (eg *Lenah Game Meats v ABC*)
 - NB Only [2] or [3] are viable possibilities – still open to argument

Full Fed Ct in *ACCC v Samton Holdings*

- Unconscientious exploitation of a party's special disadvantage (eg *Amadio*)
- Defective understanding, relationship of influence, and absence of independent explanation (eg *Garcia*)
- Unconscionable departure from previous representation (eg estoppel – *Verwayen*, *Waltons Stores v Maher*)
- Relief against forfeiture and penalty (eg *Legione v Harteley* and *Stern v McArthur*)
- Rescind contracts for unilateral mistake (eg *Taylor v Johnson*)

UC Case as Pleaded in *Optus v Telstra* (2009)

- Telstra = both Optus competitor and carrier of Optus telecommunications traffic
- Telstra therefore had access to confidential traffic data
- Telstra could use the data for competitive benefit in marketing, promotions, and planning
- Optus unaware of such use and Telstra failed to inform
- Accordingly, Optus under a ‘special disadvantage’ for UC purposes and unable through lack of notice to make a judgment about its best interests
- Telstra’s data use and other actions = unconscientious in these circumstances

Trial judge's rejection of UC case ...

- 'Novel' for Optus-like companies to claim UC
- Optus knew Telstra would see Optus traffic data
- Any disadvantage diluted by contractual restrictions on data use
- Telstra not guilty of UC simply by breaching those restrictions
- BUT ...
- Pleaded under general UC provision alone
- Reflects conventional scepticism about corporations claiming UC

Unconscionability's Interface with Corporate Law and Major Corporate Deals

- *Optus v Telstra, Bell Group v Westpac, Weston v PBL* etc litigation not the last word on raising unconscionability in corporate contexts:
 - results reinforce difficulty of dealing with unconscionability arguments at interlocutory stages
 - results influenced by available relief on other grounds
 - narrow reading of 'situational' disadvantage
 - scepticism of 'big business' claiming UC
 - conventional reading of disabling effect of disadvantage
 - heavy reliance on availability of legal advice (contrast French J in *Berbatis* litigation)
 - statutory unconscionability extends beyond special disadvantage
 - however, still a 'big ask' for corporations as victims of UC

Spigelman CJ in *A-G (NSW) v World Best Holdings* [2005] NSWCA 261

- ‘Over recent decades legislatures have authorised courts to rearrange the legal rights of persons on the basis of vague general standards which are clearly capable of misuse unless their application is carefully confined. Unconscionability is such a standard ... Unconscionability is a concept which requires a high level of moral obloquy. If it were to be applied as if it were equivalent to what is “fair” or “just”, it could transform commercial relationships.’

Competition and Consumer Act 2010 (Cth) (As of 6 June 2012)

21 Unconscionable conduct in connection with goods or services

- (1) A person must not, in trade or commerce, in connection with:
- (a) the supply or possible supply of goods or services to a person (other than a listed public company); or
 - (b) the acquisition or possible acquisition of goods or services from a person (other than a listed public company);
- engage in conduct that is, in all the circumstances, unconscionable.

Competition and Consumer Act 2010 (Cth) (*As of 6 June 2012*)

21 Unconscionable conduct in connection with goods or services

- (4) It is the intention of the Parliament that:
 - (a) this section is not limited by the unwritten law relating to unconscionable conduct; and
 - (b) this section is capable of applying to a system of conduct or pattern of behaviour, whether or not a particular individual is identified as having been disadvantaged by the conduct or behaviour; and
 - (c) in considering whether conduct to which a contract relates is unconscionable, a court's consideration of the contract may include consideration of:
 - (i) the terms of the contract; and
 - (ii) the manner in which and the extent to which the contract is carried out; and is not limited to consideration of the circumstances relating to formation of the contract.

Competition and Consumer Act 2010 1974 No. 51 (Cth) (As of 6 June 2012) (Annotations in '[]')

22 Matters the court may have regard to for the purposes of section 21 [Non-Exhaustive List of 12 Statutory Indicators of B2C and B2B UC]:

- (a) **[relative bargaining positions]** the relative strengths of the bargaining positions of the supplier and the customer; and
- (b) **[beyond legitimate commercial interests]** whether, as a result of conduct engaged in by the supplier, the customer was required to comply with conditions that were **not reasonably necessary** for the protection of the **legitimate interests** of the supplier; and
- (c) **[understanding of documents]** whether the customer was able to understand any documents relating to the supply or possible supply of the goods or services; and

Competition and Consumer Act 2010 1974 No. 51 (Cth) (*As of 6 June 2012*)

(d) [**undue influence, unfair tactics, and duress**] whether any undue influence or pressure was exerted on, or any unfair tactics were used against, the customer or a person acting on behalf of the customer by the supplier or a person acting on behalf of the supplier in relation to the supply or possible supply of the goods or services; and

(e) [**equivalent pricing and circumstances**] the amount for which, and the circumstances under which, the customer could have acquired identical or equivalent goods or services from a person other than the supplier; and

(f) [**equivalent treatment**] the extent to which the supplier's conduct towards the customer was consistent with the supplier's conduct in similar transactions between the supplier and other like customers; and

(g) [**code compliance I**] the requirements of any applicable industry code; and

Competition and Consumer Act 2010 1974 No. 51 (Cth) (*As of 6 June 2012*)

- (h) [**code compliance II**] the requirements of any other industry code, if the customer acted on the reasonable belief that the supplier would comply with that code; and
- (i) [**non-disclosure**] the extent to which the supplier unreasonably failed to disclose to the customer:
 - (i) any intended conduct of the supplier that might affect the interests of the customer; and
 - (ii) any risks to the customer arising from the supplier's intended conduct (being risks that the supplier should have foreseen would not be apparent to the customer); and

Competition and Consumer Act 2010 1974 No. 51 (Cth) *(As of 6 June 2012)*

(j) [**contractual terms, progress, and conduct**] if there is a contract between the supplier and the customer for the supply of the goods or services:

(i) the extent to which the supplier was willing to negotiate the terms and conditions of the contract with the customer; and

(ii) the terms and conditions of the contract; and

(iii) the conduct of the supplier and the customer in complying with the terms and conditions of the contract; and

(iv) any conduct that the supplier or the customer engaged in, in connection with their commercial relationship, after they entered into the contract; and

(k) [**unilateral variation**] without limiting paragraph (j), whether the supplier has a contractual right to vary unilaterally a term or condition of a contract between the supplier and the customer for the supply of the goods or services; and

(l) [**good faith**] the extent to which the supplier and the customer acted in good faith.

Sampling Views on Good Faith I

- ‘Good faith is inherent in all common law contract principles, and any attempt to imply an independent term is unnecessary and a retrograde step.’ (Carter, Peden, and Tolhurst)
- ‘(M)y present feeling is that an attempt contractually to exclude the duty to act honestly would fail [and] what foolhardy entity would be prepared to contract on that basis anyway [but] the possibility of contractually excluding an obligation to act reasonably in [the] objective sense is much more arguably open.’ (de Jersey CJ)
- ‘[Good faith is] a concept which means different things to different people in different moods at different times and in different places.’ (North American view, > 25 years ago)

Sampling Views on Good Faith II

- ‘(O)ur legal system normally achieves the result that parties should act fairly in performing a contract even if the common law does not imply a term that they act in good faith explicitly in every contract.’ (Justice James Douglas)
- ‘The mistrust of Anglo-Saxon jurists for the general concept of good faith is equalled only by the imagination which they put towards multiplying particular concepts which lead to the same result.’ (European view, quoted by Justice Douglas)

Client-Focused Analysis of GF Options

- #1: Industry standard/expectation?
- #2: Client preference/need?
- #3: Effective combination of clauses for exclusion, eg:
 - ‘entire agreement’ clause
 - ‘sole discretion’ clause
 - ‘negation of implied terms’ clause (ie not just GF?)
 - ‘no other/additional obligations’ clause
- #4: Other means/doctrines that condition exercise of contractual rights – unfair, unreasonable, and unconscientious exercises of powers and discretions
- #5: Risk of pre-execution/post-execution conduct that amounts to GF deficiency and hence statutory UC?

Multi-Level Drafting Options on GF

- Use 'choice of governing law' clause as default GF position:
 - cross-border transactions (eg law of NY)
 - Australian jurisdiction (eg NSW)
- Remain silent – leave it to the courts to imply down the track
- Impose express, general, and undefined GF obligation on some/all parties
- Impose express, general, and defined GF obligation on parties
- Define/confine GF throughout the contract:
 - Only some parties in some contexts
 - Only for some stages of the contract
- Exclude GF to the extent lawfully possible

Drafting Examples from Qld/NSW Cases

- 'The parties warrant that they shall perform all duties and act in good faith.'

Acting in good faith includes:

- (a) being fair, reasonable, and honest;
- (b) doing all things reasonably expected by the other party and by the Subcontract; and
- (c) not impeding or restricting the other party's performance.'

'This agreement contains the entire agreement of the parties with respect to its subject matter. It sets out the only conduct relied upon by the parties and supersedes all earlier conduct by the parties with respect to its subject matter.'

Contrasting Negotiating/Drafting Stances

- ‘A clear clause will embarrass the judiciary into submission ... The worry is that “good faith” may become another rule of public policy that operates outside the contract itself.’ (North American view, 20 years ago)
- ‘Commercial parties are now faced with the question of whether they dare to suggest in negotiations that they are not prepared to perform in ‘good faith’ as that may require reasonableness on their part. Alternatively, should they expressly state that they will not behave reasonably, or will that be a “deal-breaker”? (Prof Peden)
- A storm in a teacup?:
 - Sliding reasonableness/exclusion scale
 - Statutory UC trumps private agreement

Where to From Here?

- More 'test case' possibilities for advice, regulatory investigation, and litigation:
 - Will regulayors/courts flex their muscles after latest UC reforms?
 - Does general UC go beyond *Amadio/Garcia/Berbatis*?
 - Does 'situational' UC have any legs under general/statutory UC?
 - Can companies be victims of general UC?
 - Does statutory UC embrace/transcend all general UC forms?
 - Does GF mean the same under contract law and statutory UC?
- More sophistication in approaches to UC and GF:
 - nuanced client and drafting options
 - pleading GF and UC in the alternative
- Holistic approach to GF from a transactional perspective