

# HUGGINS LEGAL

## LITIGATION AND REGULATORY RISK UPDATE

EDITION 6 – 27 JANUARY 2024

### UNFAIR CONTRACT TERMS

Welcome to the sixth edition of the Litigation and Regulatory Risk Update – a newsletter for AFSL holders about developments in litigation risk (both in a Court and at AFCA) and regulatory risk.

#### 1. **What has happened?**

As of 9 November 2023, new Unfair Contract Term provisions (in the ASIC Act – **the Provisions**) came into force. The key issues being:

- (1) a breach of the Provisions exposes firms to extraordinarily high (that is, absurdly high given that the conduct at issue is about an unfair contract term) pecuniary penalties;
- (2) when a Provision is breached, a breach report must be made to ASIC (s912D of the Corporations Act); and
- (3) the test as to whether a term is unfair is vague and subjective.

#### 2. **What do I need to know about this?**

There is a great deal of material available on the internet (including at ASIC's website) about how the Provisions work, so I don't propose to focus on that issue. Instead, I will discuss how issues about the Provisions are likely to arise in practice.

ASIC will focus on large scale issues such as where an insurance company seeks to rely upon an unfair term that affects thousands of clients. For most firms, issues about the Provisions will not happen in a *vacuum* (that is, it is very unlikely that ASIC will be randomly scrutinising standard form terms and conditions and taking civil penalty proceedings where it finds a breach). Compliance with the Provisions will be an issue in the following scenarios:

- (1) A client makes an AFCA complaint and the firm, in its defence, relies upon a term that AFCA decides is unfair and therefore void (the firm will *lose* insofar as its defence relies upon that term). AFCA will publish a Determination that will come to ASIC's attention. In this scenario, the firm loses the complaint and is potentially exposed to a civil penalty because:
  - (a) It has given a client a standard form contract that contains an unfair term (there is a breach with respect to every client that had been given the contract from 9 November 2023).
  - (b) It has relied upon an unfair term.
- (2) The firm is in Court litigation with a client. The firm relies upon a term that the Court finds to be unfair and therefore void. The same circumstances apply as above except that the firm's position is worse from a regulatory risk perspective because there has been a Judgment of a Court that a term is unfair. The Court's Judgment will more readily (than an AFCA Determination) serve as the basis for ASIC regulatory action.

In either scenario, the firm would be required to make a breach report to ASIC to the effect that it had contravened a civil penalty provision (which will be an additional alert to ASIC about what has occurred). As part of this process, the firm would be expected to quantify the number of times that a standard form contract that contained an unfair term had been given to a client and/or the unfair term was relied upon.

Previously, the Provisions were not tactically important in that their effect was limited to a term being declared to be void. However, given that issues about contravening a civil penalty provision arise (and more generally because the operation of the Provisions are now better understood) the Provisions raise a significant level of risk (both the risk of losing a matter and the risk of regulatory action being taken by ASIC) for firms (and give the *other side* in AFCA matters/Court litigation an extra source of leverage in settlement negotiations). AFCA complaints and Court litigation where a firm relies upon a term in a standard form contract will inevitably cause the *other side* to look for a breach of the Provisions, thereby raising the risk that a firm could be exposed to ASIC regulatory action and that a term that the firm is relying upon could be held to be void.

### 3. **What should I do?**

The obvious first step is to review all standard form contracts and remove or modify any terms that could reasonably be said to be unfair. A firm in a dispute with a client should avoid relying upon terms that could potentially be unfair as this will put it at a tactical disadvantage (with respect to settlement negotiations – because the firm may have to settle rather than be exposed to regulatory risk - and with respect to the firm's defence) and expose the firm to ASIC regulatory action.

If you would like to discuss any of the issues raised in this Update please, of course, don't hesitate to contact me.

Regards,

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## HUGGINS LEGAL

### CAPABILITY STATEMENT

Huggins Legal has expertise in the following areas:

1. AFCA complaints concerning financial planning, stockbroking, finance broking, irresponsible lending, insurance and superannuation.
2. Financial services related litigation including disputes with advisers and disputes concerning financial services related commercial transactions.
3. Management of issues concerning adviser misconduct including breach reporting.
4. Management of issues concerning client complaints including providing advice about internal dispute resolution, breach reporting and remediation.
5. ASIC investigations.
6. AFS licensing.
7. Financial services related compliance including issues concerning the ASIC Market Integrity Rules and drafting/reviewing SOAs, FSGs and PDS'.
8. Financial services related commercial work.
9. AML/TF advice and reviews.

Huggins Legal acts for clients across Australia.