Discussion Paper: Unfair trading and Australia's consumer protection laws

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Executive Summary

Predatory businesses that systematically take advantage of vulnerable consumers are far too common. While most commerce in Australia is conducted fairly and in a way that benefits consumers, there are still many businesses that take advantage of the poorest and most vulnerable in our community. This is not about scams in which a fraudster tricks consumers, takes their money, and disappears. Nor is it about rogue traders or 'bad apples' who apply overt pressure to coerce consumers into unpalatable transactions. The focus is something more subtle, yet also more calculated. These are business models whose very operating premise relies upon taking advantage of the reduced ability of the consumers with whom it deals to protect their own interests in a transaction. Such business models include credit repair, for-profit debt negotiation, private car parks, 'car-napping', and some forms of in-home sales.

There are a range of possible legislative responses to predatory business behaviour. Governments can introduce 'bright line' rules that regulate specific business practices, such as payday loans or door-to-door sales. However, general protections that are 'standards-based' are important as well—the most relevant being the prohibitions against unconscionable conduct in various consumer laws. Standards-based rules help to fill the gaps left by bright line rules, which often struggle to keep pace with emerging predatory business models.

Consumer Action Law Centre (**Consumer Action**) has prepared this paper to inform the upcoming review of the Australian Consumer Law (**ACL**). The review provides an opportunity to consider the appropriateness of our standards around unconscionable conduct and unfair trading. This paper sets out:

- an outline of a number of business models that prey upon vulnerable consumers;
- an overview of our existing law of unconscionable conduct, and the difficulties in applying it to prevent systemic unfair trading;
- suggestions for potential improvements to our consumer protection laws, through a new standard of unfair trading; and
- an overview of the benefits such a protection can provide to consumers, business and the wider economy.

Consumer Action welcomes feedback on the directions outlined in this paper.

1. Business models that prey on vulnerable consumers

There are numerous business models that rely on unfair tactics. In each of the models discussed below, there is targeting of vulnerable consumers who may enter into a transaction that they do not fully understand and end up with a product that is unsuitable for their needs or which they can't afford. In each case, the business model itself contributes to the consumer risk.

Credit repair

Credit repair companies (CRCs) charge very high up-front fees, sometimes thousands of dollars, to 'repair' customers' credit histories. People who contact CRCs may not understand Australia's credit reporting system and are often experiencing acute financial stress. This means that they are vulnerable to high-pressure sales techniques and unrealistic promises. The promise at the centre of this business model is that CRCs will remove barriers to accessing credit, which many consumers hope will relieve financial pressure. Many Australians have little understanding of credit reporting law and believe, wrongly, that CRCs can remove legitimate listings from their credit files. Many CRCs fail to tell their clients that, in some cases, they can amend incorrect listings on their own credit reports simply by contacting their creditors directly. Instead, CRCs charge high fees for services provided free of charge by industry ombudsmen, financial counselling services and community legal centres. CRCs are also reluctant to publicise their fees and often impose large additional charges for late payment, cancellation or other 'administrative' services.

Case study 1: Credit repair

George had no knowledge about the contents of his credit report, but had concerns that his credit history may prejudice him in the future. George saw a television advertisement for a CRC, so decided to give them a call.

During his conversations with the CRC, George was told that the CRC would be able to help him, and that he would be assigned a case manager. He was told that he would need to make payment of $1,095 immediately to access the CRC's services. These claims were made by the CRC despite not having a copy of George's credit report, or knowing what was on his credit report.

Following payment, the CRC did not provide George with any services or documentation, nor was he provided a case manager as promised. In fact, even if the CRC had attempted to assist George their services would have been useless because George's credit report did not contain any default, judgment, act or bankruptcy or serious credit infringement listings. His credit report only contained one credit enquiry, which was legitimately entered.

Despite repeated requests by George for a refund, the CRC only provided a refund once Consumer Action became involved in the matter. The CRC eventually refunded George the $1,095 fee.

Consumer Action has taken legal action on behalf of consumers affected by this business model.[1] There have also been alarms raised by industry ombudsmen.[2] Academic research has provided further evidence of the need for a regulatory framework for this type of business, as the general consumer law has not inhibited the model flourishing.[3] To date, no public action has been taken by a regulator against this business type.

For-profit debt negotiators

For-profit debt negotiators or debt settlement companies promise to settle a consumer's debt for a fraction of what they owe. The idea is simple: debt settlement companies offer to negotiate down the outstanding debt (usually from credit cards or personal loans) owed to a more manageable amount so that the consumer can become debt free. Unfortunately debt settlement carries significant risks that may result in consumers becoming even worse off.

Debt settlement is an inherently risky venture: often the advice is for consumers to default on their debt which can result in fees, increased interest rates, and sometimes even legal action by creditors. Even after assuming all of this risk, consumers are offered no guarantees. In fact, some creditors refuse to negotiate with these businesses at all. Even if a settlement is reached, a consumer unable to keep up with the new settlement arrangement risks falling back into default.

These businesses regularly target their marketing efforts at those who are heavily in debt and thus vulnerable to accepting their promises. For example, these businesses purchase lists of judgment debtors or trawl court lists with details of bankruptcy and home repossession. Consumers on these lists can find themselves inundated with marketing paraphernalia and promises to "solve" their debt stress.

Case study 2: Debt negotiation[4]

Teresa had $70,000 debt in unsecured loans, including multiple credit cards and a personal loan. Teresa was suddenly unable to work because she was diagnosed with cancer. Her creditors began to harass her for late payments and she became quite stressed. She decided to sign up with a debt negotiation company, who promised to negotiate with her creditors to reduce her payments, save her from bankruptcy and stop her creditors from contacting her. The business said that they have a 100% success rate for their clients.

Teresa was charged 16% of her debts ($11,200) for the company to negotiate on her behalf. They said that she could pay this off through fortnightly payments, she only had to pay $2,000 upfront and the company would begin negotiating for her. Eighteen months later and Teresa was being harassed by her creditors again. She contacted the company to find out why this was happening and was told they have not achieved any settlements yet. Teresa was upset, but the CRC pointed out the contract she signed states that there is no guarantee of the company achieving anything for her.

[1] Consumer Action Law Centre, 'Media Release: Credit Wash 'cleans up' vulnerable consumer', 7 April 2015, available at: http://consumeraction.org.au/media-release-credit-wash-cleans-up-vulnerable-consumer/
[2] Energy & Water Ombudsman NSW, 'EWON's 'credit fix' research report raises concern', Annual Report 2012/2013, available at: http://www.ewon.com.au/index.cfm/publications/annual-reports/annual-report-20122013/feature-ewons-credit-fix-report/
[3] Ali, O'Brien and Ramsay, 'A Quick Fix? Credit Repair in Australia', *Australian Business Law Review*, Vol. 43, No. 3, pp.179-205, 2015, available at: http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2616619
[4] Case study provided by Financial Rights Legal Centre.

Teresa wants to cancel her contract but the company say she is contractually obligated to continue paying for another 18 months. Teresa was further in debt as her creditors had continued to charge interest and her creditors were threatening to take her to court. She had spent $7,600 on a service which has not done anything for her, and under her contract she still had to pay them another $5,600. Teresa tried to seek help from government agencies but she has been told there is nothing they can do and that such companies do not even need a licence.

Private car parks

Private car parks generally allow consumers to park for free for up to a certain time period, for example two hours, if they display a ticket on the car. These companies issue demands to consumers who fail to display a ticket on their car, or stay beyond the free parking period, that far exceed the value of the ticket. These demands are usually $88. This amount increases if the consumer fails to pay within 14 days. Should the consumer continue to ignore the requests for payment, the companies refer the debt to solicitors or debt collectors and further sums are demanded. Eventually court action is threatened for a sum in the region of $300. However, private car park operators do not generally have a statutory authority to 'fine' consumers, which many people are unaware of. Private car park operators base their demands for payment on an alleged breach of contract. That is, these companies say that a consumer enters into a contract to park their car in the company's car park, where it is a term of the contract to display a ticket and to pay after a certain period.

Case study 3: Private car parks

John is a student who works part time. He was driving his father's car when he parked in a private car park. John says that he did not exceed the free parking period, but received a fine in any case. John later received a 'final demand' for $88, which threatened to proceed to the Magistrates Court if he did not pay. John did not think that he had breached the contract with the car park operator but was worried about not paying the final demand in case he was taken to court.

It appears that the business model of private car parks is one that profits from the demands for payment, rather than the initial upfront charge for parking. The businesses also take advantage of a court procedure which allows someone with a potential legal claim to obtain personal details of a defendant from another person who holds that information. In this case, the car park operators use this procedure to obtain the names and addresses of individuals from roads licensing authorities.[5] It is very rare for the car park operator to sue. This personal information is used instead to make demands and threats for payment.

[5] In New South Wales, car park operators are now prevented from using this procedure - see *Road Transport Act 2013* (NSW) s 279. Victoria also recently announced that it will introduce new legislation banning private car park operators from petitioning a court to get access to a motorist's registration details and issue them with fines: http://www.premier.vic.gov.au/crackdown-on-private-carpark-operators.

Car napping

Many consumers have little understanding about their rights and obligations when involved in collisions, and they can be vulnerable to traps orchestrated by towers, repairers and debt collection lawyers.[6] At accident scenes, drivers who are 'not at fault' can be approached and offered a towing service by tow-truck drivers. They can be asked to sign paperwork to facilitate this, often at the roadside.[7] Unbeknownst to them, this paperwork may be providing the repairer with authority to store and repair a vehicle, and also an authority to a lawyer to seek recovery of costs from the 'at fault' driver. The driver may be told that the repairer is quick or cheap, or that it has a free hire car. In some cases, drivers can be told that this is a better option than involving insurance companies, because claiming may impact no-claim bonuses.

The practice has become known as 'car-napping', as the driver may later be asked to pay significant amounts for repair and storage to recover their vehicle if these amounts cannot be recovered from the other driver (or their insurer). The practice can impact the 'at fault' driver as well, when they or their insurance company are targeted with inflated claims for the cost of repairs. In some instances, this results in court action initiated by the lawyer acting on behalf of the 'not at fault' driver, commonly without the full knowledge of that driver.

Case study 4: Car napping

Peter was involved in a car accident, and was the 'at fault' driver. Peter swapped contact details with the other driver, although there was only a small amount of damage to the other driver's car. Peter made a claim with his insurer to cover the damage to his vehicle, which was repaired. He thought the matter was dealt with until he received a Magistrates' Court complaint from a law firm acting for the other driver claiming approximately $30,000 in damages. Peter claims the damage he caused to the other vehicle would not have cost more than $10,000 to repair. It appears that the 'not at fault' driver had signed an authority to act which enabled a lawyer to seek recovery from Peter or his insurer.

Because the amount claimed was excessive, there was some dispute between Peter's insurer and the law firm, which resulted in a judgment being entered against Peter. This caused Peter much stress and anxiety, particularly given that the judgment could have resulted in potential enforcement action and a negative listing on his credit report.

In-home sales

The products sold through high pressure in-home sales have varied from encyclopaedias to vacuum cleaners and educational software. Most recently this technique has included vocational education. Often, the products are sold on credit arrangements, which can lead to debt problems.

There are various factors associated with in-home sales that mean consumers are more vulnerable to tactics that impede their rational judgment. For example, research has found that a consumer may be under greater pressure where an

[6] Eamonn Duff, 'Rogue towers accused of 'carnapping' scam', *The Age*, 17 May 2015, available at: http://www.theage.com.au/victoria/rogue-towers-accused-of-carnapping-scam-20150516-gh335h.html
[7] For example: http://www.ecollect.com.au/debts/_blocks/motor.accident.instructions_Melbourne.pdf

'invitation' into the home has been made by the consumer. The act of agreeing to be contacted makes it more likely that a consumer will comply with a larger request later, for example, buying the product or service being sold.[8] The same research also found that there is a strong social element associated with in-home sales. By being in the home, the salesperson obtains information about a person's family or lifestyle, enabling them to exert authority or enhance understanding, liking or similarity.

There can also be huge psychological barriers to backing out of a transaction once a consumer has committed to a visit, and invited the salesperson into their home. For example, asking someone to leave your house after you have invited them in is substantially more difficult than walking out of a retail store. Simply saying 'I am not interested' and walking away is not a realistic option when someone is in your home.

The 'foot in the door' effect is also powerful. Consumers can be asked a number of questions where the answer is obviously 'yes'. 'Wouldn't you like to improve your jobs skills?', for example. The offering of something 'free' is like the icing on the cake—statements like 'you don't have to pay upfront', or inducements like a free computer, can focus the mind on the initial benefit, rather than the longer-term debt. This can all contribute to the purchase of an item that is not suitable, wanted or affordable.

[8] Consumer Action Law Centre and Deakin University, 'Policy report: An analysis of the psychology of in-home sales of educational software', 1 March 2010, available at: http://consumeraction.org.au/policy-report-an-analysis-of-the-psychology-of-in-home-sales-of-educational-software/

2. Current legal standard: unconscionable conduct

The development of the prohibition on unconscionable conduct

The primary standards-based rules to protect vulnerable consumers are the prohibitions against unconscionable conduct. The law of unconscionable conduct has its roots in the doctrines of the courts of equity, developed over the course of several centuries, to do what justice required in cases where the strict application of the law would be unduly harsh.[9] In Australia, the two key cases of *Blomley v Ryan*[10] in 1956 and *Commercial Bank of Australia Ltd v Amadio*[11] in 1983 set the tone of the judge-made law on unconscionable conduct, with may be characterised as addressing a situation where one party to a transaction is at a special disadvantage in dealing with the other, and the other party then 'unconscientiously takes advantage of the opportunity thus placed in his hands'.[12]

Prohibitions against unconscionable conduct became part of the statutory consumer protection regime in 1986, and were later introduced into a range of other legislation including the *Australian Securities & Investments Commission Act 2001* (Cth) (**ASIC Act**). The relevant provisions were initially introduced into the *Trade Practices Act 1974* (repealed), but are now part of the Australian Consumer Law (**ACL**).[13]

The ACL has two substantive provisions relating to unconscionable conduct.[14] The first prohibits unconscionable conduct 'within the meaning of the unwritten law from time to time'. The courts have not settled on what constitutes such conduct, but it is generally understood to refer to the situations described in *Blomley* and *Amadio*.

The second prohibition, often referred to as 'statutory unconscionable conduct', is a broader concept.[15] For example, the prohibition now states:

- it is not limited by the unwritten law relating to unconscionable conduct; and
- it 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
- it is not limited to conduct relating to the formation of a contract, and consideration may be given to the terms of the contract and the manner in which and the extent to which the contract is carried out.

The ACL also sets out a list of factors to which the court may have regard when considering whether there has been statutory unconscionable conduct, including the relative bargaining positions of the parties, and whether the consumer was

[9] Many of the early cases concerning what could be described as unconscionable conduct focused on 'catching bargains', or deals struck between moneylenders and expectant heirs at usurious rates of interest. For an account of the development of the law of unconscionable conduct generally see Carter, JW, Peden, E and Tolhurst, GJ, *Contract Law in Australia* (5th ed, 2007), pages 517-9.

[10] *Blomley v Ryan* (1956) 99 CLR 362.

[11] *Commercial Bank of Australia Ltd v Amadio* (1983) 151 CLR 447.

[12] *Blomley v Ryan* (1956) 99 CLR 362 at 415, per Kitto J.

[13] Schedule 2 - The Australian Consumer Law, *Competition & Consumer Act 2010* (Cth).

[14] These provisions are replicated in the ASIC Act in relation to financial services.

[15] Schedule 2 - The Australian Consumer Law, *Competition & Consumer Act 2010* (Cth), s 21.

under influence or pressure.[16] This is not an exhaustive list. This provision, however, does not have a settled legal meaning.

Confusion in the courts: the unsettled meaning of statutory unconscionable conduct

Various federal and state judiciaries have wrestled with the statutory concept of 'unconscionable conduct' and have arrived at different interpretations. The High Court is yet to consider the statutory prohibition in any depth, meaning confusion is likely to reign in the lower courts for some time yet.

In *Attorney General (NSW) v World Best Holdings Ltd,*[17] Chief Justice Spigelman found that 'moral obloquy' needed to be found in order for conduct to be 'unconscionable'.[18] Experts have lamented the fact that this influential decision did not interpret the unconscionable conduct provisions in the manner 'that reflects the intention of Parliament, both at the time of the introduction of the original pieces of legislation, as well as the amendments which were intended to enhance its operation.'[19]

A number of subsequent judgments have accepted the proposition that unconscionable conduct must involve 'moral obloquy'. Regulators and consumer advocates were heartened by an apparent breaking of the mould in *Australian Competition and Consumer Commission v Lux Distributors Pty Ltd*[20] in which the Full Federal Court diminished the importance of the concept of moral obloquy. While noting that moral obloquy or moral tainting might be relevant, the Court ruled that the court should be concerned with 'conduct against conscience by reference to the norms of society that is in question.' This approach has been followed in other Federal Court decisions, such as *Australian Competition and Consumer Commission v Coles Supermarkets Australia Pty Ltd*[21] and *Paciocco v Australian and New Zealand Banking Group Ltd.*[22]

However, the Victorian Supreme Court of Appeal decision of *Director of Consumer Affairs (Vic) v Scully (No. 3)* (**the Scully decision**)[23] reverted to the narrower and restrictive interpretation by requiring moral obloquy once again. This approach has been followed by subsequent Victorian Supreme Court cases, including *DPN Solutions Pty Ltd v Tridant Pty Ltd*[24] and *Sgargetta v National Australia Bank Ltd.*[25]

It is clear that two differing lines of authority are developing around the meaning of unconscionable conduct in the Federal Court and Victorian Supreme Court, again demonstrating the difficulty of applying this imprecise concept. In fact, the Full Federal Court has acknowledged that it is futile to attempt to define the concept of unconscionable conduct, saying:

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[16] Schedule 2 - The Australian Consumer Law, *Competition & Consumer Act 2010* (Cth), s 22.
[17] *Attorney General (NSW) v World Best Holdings Ltd* [2005] 63 NSWLR 557.
[18] Prof. Bob Baxt, 'A clear definition', *Company Director*, May 2015, p. 58.
[19] Herbert Smith Freehills, Submission to the Harper Competition Policy Review, July 2014, p. 3, available at: http://competitionpolicyreview.gov.au/files/2014/07/Baxt.pdf
[20] *Australian Competition and Consumer Commission v Lux Distributors Pty Ltd* [2013] FCAFC 90.
[21] *Australian Competition and Consumer Commission v Coles Supermarkets Australia Pty Ltd* [2014] FCA 1405.
[22] *Paciocco v Australian and New Zealand Banking Group Ltd* [2015] FCAFC 50.
[23] *Director of Consumer Affairs (Vic) v Scully (No. 3) [*2013] VSCA 292.
[24] *DPN Solutions Pty Ltd v Tridant Pty Ltd* [2014] VSC 511.
[25] *Sgargetta v National Australia Bank Ltd* [2014] VSCA 159.

> *'…any agonised search for definition, for distilled epitomes or for short hands of broad social norms and general principles will lead to disappointment, to a sense of futility, and to the likelihood of error. The evaluation is not a process of deductive reasoning predicated upon the presence or absence of fixed elements or fixed rules.'*[26]

Some judges (or arguably the majority of judges) appear to believe that the statutory prohibition 'could result in the transformation of commercial relationships in a manner which… was not the intention of the legislation.'[27] This concern appears to have unnecessarily limited the application of the prohibition against unconscionable conduct in some courts to those cases that involve 'moral obloquy'. This sentiment appears to be shared by the High Court, with the Court in *Kavakas v Crown Melbourne Limited* toying with the idea that moral obloquy was relevant in evaluating unconscionability, although not deciding the matter.[28]

Without legislative change, the two lines of authority developing in the courts are likely to continue to water down the effectiveness of the prohibition against unconscionable conduct, leaving unacceptable gaps in consumer protection laws.

[26] *Paciocco v Australian and New Zealand Banking Group Ltd* [2015] FCAFC 50 at [304].
[27] *Attorney General (NSW) v World Best Holdings Ltd* [2005] 63 NSWLR 557 at [121].
[28] *Kavakas v Crown Melbourne Limited* (2013) 250 CLR 392.

3. The limitations of unconscionable conduct

Despite the prohibition on unconscionable conduct, we still see business models that profit from taking advantage of vulnerable consumers. Why hasn't the prohibition prevented or inhibited this type of trading?

Unconscionable is not the same as unfair

The key problem is that the unconscionable conduct provisions do not actually prohibit unfair trading. The Federal Court recently stated that 'conduct which is unfair or unreasonable is not for those reasons alone unconscionable'.[29] The prohibition imposes a high threshold before conduct will be considered 'unconscionable'.

This high threshold makes it difficult for regulators to take action against traders that test the boundaries. In a submission to a 2013 Senate Inquiry, the Australian Securities & Investments Commission (**ASIC**) stated:

> *'The courts have set a high bar for establishing unconscionability, particularly for commercial transactions. Whether a specific transaction is unconscionable depends on the individual facts and circumstances of the case. A general power imbalance between parties or a contract that favours one party more than the other is not sufficient to support a claim of unconscionable conduct'.*[30]

The Productivity Commission also acknowledged in 2008 that the prohibition of unconscionable conduct in the generic legislation represents a prohibition of unfairness, but usually only unfairness that crosses a high threshold of severity. Other provisions deal with specific instances of misconduct, and fail to keep pace with the 'innovation' of traders.[31]

The law is uncertain

As noted above, the law of unconscionable conduct is still unclear, with courts unable to agree on an interpretation of the statutory prohibition. While the Federal Court has considered accepted '**norms of society**' as the standard for determining unconscionable conduct, other courts have required a higher standard of 'moral obloquy'.

The effect of litigation in a variety of related contexts in differing courts has resulted in a 'smorgasbord' of untested issues for advice, litigation, and other regulatory action.[32] There is little direction given to courts in how to mediate between these different possible understandings of what amounts to unconscionable conduct and little explanation of how a breach of the statutory

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[29] *Australian Competition and Consumer Commission v ACN 117 372 915 Pty Ltd (in Liq) (formerly Advanced Medical Institute Pty Ltd)* [2015] FCA 368 at [39].
[30] Australian Securities and Investments Commission, 'Senate Inquiry into the performance of the Australian Securities and Investments Commission - Submission by ASIC on reforms to the credit industry and 'low doc' loans, October 2013, p. 6.
[31] Productivity Commission, 'Review of Australia's Consumer Policy Framework - Productivity Commission Inquiry Report', Volume 2, 30 April 2008, p. 140.
[32] Prof. Bryan Horrigan, 'New Directions in How Legislators, Courts, and Legal Practitioners Approach Unconscionable Conduct and Good Faith', draft as of 15 October 2012, p. 2, available at: http://www.law.uq.edu.au/documents/cli-sem-series/2012/Horrigan-paper-18-10-12.pdf

prohibition might be assessed.[33] This has resulted in the development of (at least) two differing judicial lines of authority. The uncertainty of the law makes it difficult for consumers to rely on, and difficult for regulators to enforce.

Difficulties in enforcement: relying on vulnerable witnesses

ACL regulators face significant hurdles in enforcing the prohibition against unconscionable conduct, which stem from the uncertainty of the law and that courts focus on individual cases, rather than systemic unfair conduct. This limits the evidence upon which the regulator can rely, and often means the affected consumers must be willing to take the stand as witnesses.

Vulnerable and disadvantaged consumers raise particular challenges for enforcement activity. They are often less willing to complain, more easily intimidated, less likely to have retained documentary records and less likely to perform well as witnesses in court proceedings where among other things they can be readily confused under skilled cross examination.[34] Often vulnerable consumers will be members of a class of consumers who have suffered a loss, and it is obviously asking a lot of an individual to participate in lengthy and complicated court enforcement processes when there may be limited benefit to them individually.

As such, regulators can be less willing to take on cases affecting vulnerable and disadvantaged consumers that significantly rely on individual consumer testimony. In the regulators' defence, courts and the rules of evidence are not generally open to approaches that may ameliorate the impact on vulnerable consumers.

Difficulties in enforcement: complex business models

Where there are complex business models with a number of parties in a supply chain, even where unconscionable conduct is found, some key actors can escape liability. This limits the ability of the prohibition to have a systemic effect on these more complex business models. This was a notorious problem in relation to finance broking before the enactment of the *National Consumer Credit Protection Act 2009* (Cth), where lenders could not be found responsible for the unconscionable conduct of brokers. These difficulties are demonstrated by the Western Australia Supreme Court's decision in *Perpetual Trustee Company v Burniston (No. 2)*.[35]

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[33] Jeannie Paterson and Gerard Brody, '"Safety Net" Consumer Protection: Using Prohibitions on Unfair and Unconscionable Conduct to Respond to Predatory Business Models", *Journal of Consumer Policy*, published online 9 November 2014.

[34] The difficulties faced by some vulnerable witnesses have been recognised by the Australian Law Reform Commission (ALRC) in their report into the Uniform Evidence Law. The ALRC noted that some cross-examination techniques "can adversely affect the ability of a person with an intellectual disability to recall an event accurately, and repetition of questions can cause a person with an intellectual disability to change his or her answers. This may result in the witness giving the questioner a response which the questioning process has led the witness to perceive to be the 'correct' answer, even though the witness may effectively be agreeing to something which is not true." Australian Law Reform Commission, *Uniform Evidence Law (ALRC Report 102)*, Chapter 5, 8 February 2006, available at: http://www.alrc.gov.au/publications/5.%20Examination%20and%20Cross-Examination%20of%20Witnesses%20/examination-witnesses. This may often also be true of consumers with other forms of disadvantage or vulnerability.

[35] *Perpetual Trustee Company v Burniston (No. 2)* [2012] WASC 383, as quoted in: Australian Securities and Investments Commission, 'Senate Inquiry into the performance of the Australian Securities and Investments Commission - Submission by ASIC on reforms to the credit industry and 'low doc' loans, October 2013, pp. 26-27.

Perpetual Trustee Company v Burniston (No. 2)

Following the sale of their home in 2008, the borrowers invested $235,000 of the proceeds with a mortgage broker who also arranged a loan for the borrowers to purchase a new residence. The broker promised that the investment returns would cover the loan repayments. The loan was made on the basis of a low doc loan application that contained misrepresentations made by the broker, including that the loan was for business purposes, that the borrowers were self-employed and that they had substantial income.

The Court found that there was unconscionable conduct on the part of the broker due to the false representations in the loan application and the manner in which the broker had the borrowers execute the loan documents, including not advising the borrowers of the false representations made or warning them of the risk of loss.

However, the Court found that the lender had not engaged in unconscionable conduct, either indirectly through the broker or directly in its own right because the lender owed no duty of care to the borrowers, and the failure to check the accuracy of information, or take reasonable precautions, might have been careless but was not unconscionable.

Similar problems occurred in the *Scully* decision, where individual directors behind the offending business structure were found to have not engaged in unconscionable conduct.

The term 'unconscionable' is confusing

Ask an average business owner or consumer what the phrase 'unconscionable conduct' means and you are likely to get a blank stare in response. This is no surprise, given that almost half of all Australians aged between 15 and 74 years have literacy skills below level 3. Level 3 is considered the minimum level required to meet the increasingly complex demands of a knowledge society like Australia.[36]

In *Attorney-General NSW v World Best Holdings Ltd*, Chief Justice Spigelman expressed the view that unconscionability is a concept with which judges have particular experience.[37] Unfortunately, this experience is not shared by the wider community. Business people deciding whether to pursue a particular marketing strategy should not have to delve into case law to discover whether that strategy will operate within the limits of the law. Nor should a consumer have to consider the interplay between equity and statute law when determining whether they have a remedy against a dodgy trader. 'Unconscionable' is not a word commonly used in ordinary conversation, and makes it difficult for businesses and consumers alike to recognise when conduct may be 'unconscionable'.

The broader market does not respond to enforcement action

The statutory prohibition on unconscionable conduct in Australian consumer law has at times been criticised by academics as incapable of addressing 'systemic or widespread issues'.[38] This concern has been echoed by ASIC:

[36] Australian Bureau of Statistics, 'Adult Literacy', 23 July 2008, available at: http://www.abs.gov.au/AUSSTATS/abs@.nsf/Lookup/4102.0Chapter6102008
[37] *Attorney General (NSW) v World Best Holdings Ltd* [2005] 63 NSWLR 557 at [122].
[38] Jeannie Paterson and Gerard Brody, '"Safety Net" Consumer Protection: Using Prohibitions on Unfair and Unconscionable Conduct to Respond to Predatory Business Models", *Journal of Consumer Policy*, published online 9 November 2014.

'[the unconscionable conduct provisions] are dependent on the particular facts and circumstances of individual cases. Findings that they have been breached tend to be specific to the case at hand and rarely set a general rule or precedent. The conduct standards in the ASIC Act were therefore at best an imperfect tool for a regulator seeking to address systemic or widespread issues.'[39]

In line with these observations, we have seen little response from the broader market when traders are successfully prosecuted for engaging in unconscionable conduct. The cases below are examples of significant 'wins' for regulators and consumers that have failed to achieve systemic change:

Walker v DTGV1 Pty Ltd[40]

The Victorian Civil and Administrative Tribunal (VCAT) found that DTGV1 Pty Ltd (Motor Finance Wizard), amongst other things, had engaged in unconscionable conduct and engaged in misleading or deceptive conduct in breach of the *Fair Trading Act 1999* (Vic). VCAT expressed particular concern about 'the length of the stay at the dealership, the delay in clearly explaining what the nature of the transaction was, the speed and inadequacy of explanations of the transaction given, the lack of real choice in car selection, and the lack of real opportunity given to read or understand the consumer lease'. Despite this decision, we have seen Motor Finance Wizard and many other motor car lease businesses continue to operate with largely the same business model.

Australian Competition and Consumer Commission v Titan Marketing Pty Ltd[41]

Titan Marketing sold first aid kits and water filters through door to door sales, including to consumers in Indigenous communities of Far North Queensland and the Northern Territory. In June 2014, Titan was ordered by the Federal Court, by consent, to pay total penalties of $750,000 for engaging in unconscionable conduct and making false and misleading representations, among other contraventions. In February 2014, ASIC accepted an enforceable undertaking with Home Essentials Australia Pty Ltd (and others) for similar conduct.[42] Despite these cases, pushy sales tactics are still being used in Indigenous communities, particularly with products such as consumer leases, funeral insurance and payday loans.

[39] Australian Securities and Investments Commission, 'Senate Inquiry into the performance of the Australian Securities and Investments Commission - Submission by ASIC on reforms to the credit industry and 'low doc' loans, October 2013, p. 6.
[40] *Walker v DTGV1 Pty Ltd trading as V1 Leasing (Credit)* [2011] VCAT 880 (12 May 2011).
[41] *Australian Competition and Consumer Commission v Titan Marketing Pty Ltd* [2014] FCA 913.
[42] Australian Securities and Investments Commission, Media Release 14-021MR Unlicensed rental companies enter into enforceable undertaking with ASIC, 4 February 2014, available at: http://asic.gov.au/about-asic/media-centre/find-a-media-release/2014-releases/14-021mr-unlicensed-rental-companies-enter-into-enforceable-undertaking-with-asic/

Australian Securities and Investments Commission v The Cash Store Pty Ltd[43]

The Federal Court found that payday lender The Cash Store had engaged in unconscionable conduct by selling consumer credit insurance (CCI) with its loans that was unlikely to ever provide any benefit to their customers.[44] The majority of The Cash Store's customers were low income earners, or in receipt of Centrelink benefits. While the behaviour in The Cash Store case was particularly bad, the technique used by The Cash Store of promoting the insurance as an 'add-on' late in the sale is used to sell CCI, gap insurance and motor vehicle warranties every day. Despite the Federal Court handing down a $1.1 million penalty to The Cash Store for selling the insurance (the maximum available), the insurers involved agreeing to refund $2.4 million in premiums, and a growing body of evidence linking the add-on mechanism to consumer detriment, 45 insurers still allow intermediaries to sell their products in this way.

[43] *Australian Securities and Investments Commission v The Cash Store Pty Ltd (in liq)* [2014] FCA 926 and *Australian Securities and Investments Commission v Cash Store Pty Ltd (in liq) (No 2)* [2015] FCA 93.
[44] Australian Securities and Investments Commission, '14-220MR Payday lender engages in unconscionable conduct and breaches consumer credit laws', 2 September 2014, available at: http://asic.gov.au/about-asic/media-centre/find-a-media-release/2014-releases/14-220mr-payday-lender-engages-in-unconscionable-conduct-and-breaches-consumer-credit-laws/
[45] For example, see Financial Conduct Authority, 'MS14/1 General Insurance Add-Ons: Final Report – Confirmed Findings of the Market Study', 24 July 2014, paragraph 1.6, available at: https://www.fca.org.uk/your-fca/documents/market-studies/ms14-01-final-report.

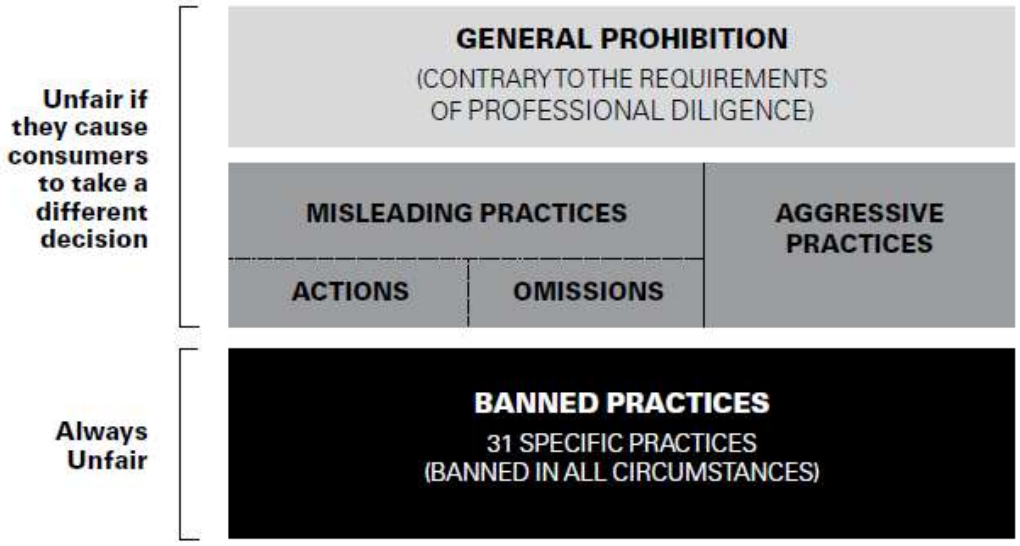
4. Extending unconscionable conduct

For many years, there has been discussion in Australia of the possibility of extending the prohibition on unconscionable conduct to form a prohibition on unfair trading. In 2008, the Productivity Commission acknowledged that it would be 'prudent' for Australian policymakers to see how the European model developed, and consider the option of pursuing a general unfair practices provision.[46]

The European Union Directive

In 2005, the European Union adopted the Unfair Commercial Practices Directive (**the EU Directive**) to boost consumer confidence and make it easier for businesses to carry out cross border trading.[47] The EU Directive takes a three-tired approach which consists of a general prohibition of unfair commercial practices, prohibitions against misleading and aggressive practices, and 31 specific practices that are prohibited in all circumstances.[48]

FIGURE 1: Unfair Commercial Practices Directive



***Source**: UK Office of Fair Trading, 'Consumer Protection From Unfair Trading', 2008, available at: www.gov.uk/government/uploads/system/uploads/attachment_data/file/284442/oft1008.pdf*

A business will contravene the first tier, being the general prohibition of unfair commercial practices, if:

- it is not professionally diligent; and

[46] Productivity Commission, 'Review of Australia's Consumer Policy Framework - Productivity Commission Inquiry Report', Volume 2, 30 April 2008, p. 141.
[47] European Commission, 'Unfair commercial practices directive', accessed 8 July 2015, available at: http://ec.europa.eu/consumers/consumer_rights/unfair-trade/unfair-practices/index_en.htm
[48] UK Office of Fair Trading, 'Consumer Protection From Unfair Trading', 2008, available at: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/284442/oft1008.pdf

- it materially distorts, or is likely to materially distort, the economic behaviour of the average customer.

Economic behaviour will be 'materially distorted' if, for example, the average consumer would buy a product they would not otherwise have bought, or would not exercise cancellation rights when otherwise they would have done so.[49]

The second tier of the EU Directive prohibits commercial practices that are misleading (whether by act or omission) or aggressive, and which cause (or are likely to cause) the average consumer to take a different decision. A commercial practice will contravene the prohibition on misleading omissions if the practice:

> omits or hides material information, or provides it in an unclear, unintelligible, ambiguous or untimely manner; and
> the average consumer takes, or is likely to take, a different decision as a result.

The prohibition of aggressive practices focuses on the existence of undue influence, and the impact this has on the average consumer's freedom of choice. A commercial practice will be 'aggressive' if, by harassment, coercion or undue influence, it:

> significantly impairs, or is likely to significantly impair, the average consumer's freedom of choice or conduct concerning the product; and
> the average consumer takes, or is likely to take, a different decision as a result.
>
> These prohibitions facilitate consideration of insights from behavioural economics, as they target businesses that exploit the inherent behavioural biases of consumers. This is a key element that Australia's unconscionable conduct provisions lack.

A broader unfair trading provision for Australia

Conceptually, a broad provision against unfairness that takes into account principles of behavioural economics is attractive because it may 'future-proof' legislation, and can fill the gaps left by the current unconscionable conduct provisions.

Drawing on the EU directive, there are three ways in which Australia's existing prohibition could be enhanced:

- being more specific about aggressive market practices;
- extending to misleading omissions; and
- becoming prospective.

Defining aggressive market practices

The first enhancement might involve defining aggressive market practices—not as in specific conduct or practices, but in terms of the effect of such practices on consumer decision-making. This picks up on the EU Directive's focus on conduct that 'materially distorts the economic behaviour of the average consumer' or

[49] UK Office of Fair Trading, 'Consumer Protection From Unfair Trading', 2008, paragraph 3.4, available at: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/284442/oft1008.pdf

'significantly impairs the average consumer's freedom of choice or conduct'. Rather than focusing on whether the conduct offends conscience, such analysis can bring in consideration of consumers' behavioural biases that might be exploited by traders. For example, tactics used by some in-home salespeople that make it more likely that a consumer will sign up may be caught. Also, framed in this way, the prohibition is more likely to be pro-competitive, as it promotes consumer choice.

Extending prohibition on misleading omissions

The second enhancement relates to misleading omissions. The ACL's existing prohibition on conduct that is misleading or deceptive, or conduct that is likely to mislead or deceive, does extend to some misleading omissions. However, the EU Directive's approach which covers practices which 'omit or hide material information, or provides it in an unclear, unintelligible, ambiguous or untimely manner' is likely to be broader.

The recent case of *Australian Competition and Consumer Commission v AGL South Australia Pty Ltd*[50] provides an example. The case concerned the marketing practices of energy retailer, AGL, and the way it marketed its energy plans on the basis of the discounts that were offered. Following many consumers signing up to the energy plans, AGL raised the price from which the 'discounts' were based. The ACCC alleged that communications to customers about these price rises were misleading. There were two communications in relation to two separate groups of customers. For the first, the court found misleading conduct because the communication stated that the consumers' discount remained (it did not, because it was effectively lost through the price rise). In relation to the second communication, however, the Court did not find any misleading conduct. That was because there was nothing in that letter stating that the discount would continue.

The ACCC argued that AGL had a positive obligation to disclose to the customers at the time of the increase that their discounts would be lost but the Court did not agree that this was required. The Court stated the ACCC had shown no basis for a conclusion that the customers had an interest in being informed of the particularised details—there was no 'reasonable expectation for disclosure'.[51]

Prohibiting omissions that hide material information, or provide information in an unclear, unintelligible, ambiguous or untimely way, would require traders to bring much more clarity to their marketing and business practices.

Making the prohibition prospective

The final enhancement would be to make the prohibition prospective. Currently, the prohibition on unconscionable conduct applies to past conduct. This contrasts to the EU Directive where the prohibition includes conduct that 'is likely to' significantly impair the average consumer's freedom of choice or conduct concerning the product or 'is likely to' result in the average consumer making a different transaction decision. This approach aligns with the ACL prohibition on conduct that 'is likely to' mislead or deceive. Such an approach may mean that a regulator does not need to prove that the conduct occurred and harm resulted. It may also mean that the regulator does not need to rely on vulnerable witnesses.

[50] *Australian Competition and Consumer Commission v AGL South Australia Pty Ltd* [2014] FCA 1369.
[51] *Miller & Associates Insurance Broking Pty Ltd v BMW Australia Finance Limited* [2010] HCA 31.

Instead, a broader range of evidence could be considered, including survey evidence or evidence from experts about consumer decision-making. This approach might also allow a regulator to be more proactive in the prevention of harm.

The benefits of such a provision are set out more fully below.

5. The benefits of a general unfair practices provision

The benefits of introducing a general unfair practices provision extend beyond providing better protections to consumers. Such a provision would be easier for regulators to enforce, provide more legal certainty, and increase consumer confidence and market equality.

Economic benefits

In the absence of legal protection, consumers bear the cost and risk themselves when they encounter traders who deal with them unfairly. Essentially, there is a transfer in value and wealth from consumers to the trader who has dealt with them unfairly. There is a clear economic benefit in reversing this transfer of wealth to ensure that unfair traders bear the costs of their behaviour by requiring them to modify their conduct and be liable for such behaviour. It is unreasonable to deny consumers a remedy and to permit suppliers to engage in unfair conduct just so these traders can avoid the costs of conducting themselves more fairly.[52]

In its submission to the Productivity Commission in 2008, the Queensland Government stated that for some consumers, unfair practices and even small transactions costs limit their ability to realise the benefit of competitive markets.[53] This results in suboptimal allocation of risk. Differing degrees of disadvantage means that risk is being unevenly felt across society. The Productivity Commission has also made the case that allowing market misconduct to occur without redress can be anti-competitive in that it gives legally non-compliant traders an advantage over those that do comply.[54]

Improving consumer protections is also likely to increase consumer confidence, as was seen in the European Union where the European Commission found that the high level of consumer protection set by the EU Directive appeared to be helping boost consumers' confidence.[55] Lower risks for consumers would encourage consumers to trust new firms and products, stimulating innovation and productivity growth and reduce the transactions costs consumers incur to avoid risk. There would be other intangible benefits that come from fairer outcomes, not least being the reduced emotional distress from purchases that do not work out as expected.

Allowing consumers and 'fair' businesses to absorb the cost of the practices of unfair traders does not make economic sense. For those businesses already operating fairly and in good faith, the introduction of such a provision is unlikely to mean such businesses will have to make major changes to their practices.[56]

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[52] New Zealand Consumer Affairs, 'Consumer Law Reform Additional Paper: Unconscionability', October 2010, available at: http://www.consumeraffairs.govt.nz/legislation-policy/policy-reports-and-papers/discussion-papers/consumer-law-reform-additional-paper-2013-october-2010-unconscionability.

[53] Queensland Government, 'Response to Productivity Commission Issues Paper: Consumer Policy Framework', May 2007, available at: http://www.pc.gov.au/inquiries/completed/consumer-policy/submissions/sub087.pdf.

[54] Productivity Commission, 'Review of Australia's Consumer Policy Framework — Inquiry Report 45', Volume 2, April 2008, p. 193, available at: http://www.pc.gov.au/projects/inquiry/consumer/docs/finalreport.

[55] European Commission, 'Report from the Commission to the European Parliament, the Council and the European Economic and Social Committee, 14 March 2013, p. 30, available at: http://ec.europa.eu/justice/consumer-marketing/files/ucpd_report_en.pdf

[56] UK Office of Fair Trading, 'Consumer Protection From Unfair Trading', 2008, paragraph 3.4, available at: https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/284442/oft1008.pdf.

Easier for regulators to enforce

Predatory businesses set themselves up on the basis of gaining profits from their unfair business models. These are whole of business models that require a suite of tools, including crooked marketing, aggressive sales tactics and targeting of vulnerable communities, to succeed. The difficulty with the current prohibition of unconscionable conduct is that it focuses on individual incidents of misconduct, rather than entire business models. Regulators are forced to act after misconduct has occurred in order to establish the basis for a claim, and must prove a high threshold of misconduct in order to substantiate a claim.

However, a general unfair practices provision would enable regulators to prosecute traders based on their business models, rather than focus on individual incidents of misconduct. According to the European Commission, the EU Directive has enabled enforcement agencies:

> *'to curb a broad range of unfair business practices, such as providing untruthful information to consumers or using aggressive marketing techniques to influence their choices. Its legal framework is proving well suited to assess the fairness of the new online practices that are developing in parallel with the evolution of advertising sales techniques'.*[57]

The addition of the phrase 'is likely to' will also enable regulators to intervene before significant harm has occurred, rather than engage in late-stage intervention strategies. The inclusion of the term 'is likely to' will empower the regulator to take proactive enforcement action, as has been seen by the inclusion of this term in ASIC powers to refuse financial services licences in the Future of Financial Advice reforms. Under section 913(1)(b) of the *Corporations Act 2001*, ASIC can now refuse a licence if it believes the applicant is 'likely to contravene' its obligations as a licensee under section 912A. According to the Explanatory Memorandum for this amendment, '[t]his new formulation is designed to ensure that ASIC can more appropriately account for the likelihood or probability of a future contravention'.[58] Similar logic would apply to a proscriptive general unfair practices provision.

Ensures consumer protection reflects community standards

The standard for unfair trading would be linked to the distortion of economic behaviour, which is more certain than the morally-rooted concepts of 'unconscionability' and 'moral obloquy'. The term 'unfair' makes much more sense to consumers and traders, and would allow them to make at least a general assessment of the likely lawfulness of conduct themselves. This could have clear compliance benefits.

Studies in behavioural economics have shown that we have an intuitive understanding of standards of fair dealing and that this is an important value in our interactions with other people.[59] Even an intuitive view provides a starting point for

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[57] European Commission, 'Unfair commercial practices directive', accessed 8 July 2015, available at: http://ec.europa.eu/consumers/consumer_rights/unfair-trade/unfair-practices/index_en.htm.

[58] *Corporations Amendment (Future of Financial Advice) Bill 2012* (Cth), Revised Explanatory Memorandum, paragraph 2.22.

[59] Ian Macauley, *You can see a lot by just looking: Understanding human judgement in financial decision-making*, Centre for Policy Development, October 2008, p 30-32, available at http://cpd.org.au/wp-content/uploads/2008/10/CPD_OP5_Ian_McAuley_Behavioural_Economics_Web2.pdf.

self-reflection for businesses about whether a proposed course of conduct is likely to offend community values and the statutory safety net prohibitions.[60]

[60] Jeannie Paterson and Gerard Brody, '"Safety Net" Consumer Protection: Using Prohibitions on Unfair and Unconscionable Conduct to Respond to Predatory Business Models", *Journal of Consumer Policy,* published online 9 November 2014.

6. Conclusion

Predatory business models that unfairly target vulnerable consumers have managed to slip through the cracks of our current consumer protection laws. These are not necessarily 'scams'. In fact, these business models are usually far more subtle. Their operating premise relies on taking advantage of consumers who have a reduced ability to protect their own interests. These business models range from credit repair companies and for-profit debt negotiators, to 'car napping' tow truck drivers and some door-to-door sales.

The unconscionable conduct provisions have enabled enforcement action against many very sharp business transactions. However, the prohibition on unconscionable conduct has failed to disrupt business models that are 'unfair'. The unconscionable conduct provisions are generally unable to prevent systemically unfair conduct, as findings of unconscionable conduct tend to be specific to the case at hand and rarely set a general rule or precedent. The judiciary are also unable to agree on how to interpret the provisions, making it difficult for regulators, businesses and consumers to know when conduct will be 'unconscionable'.

The upcoming review of the ACL is an opportunity to seal the gaps in our consumer protection laws that allow these unfair business models to thrive. The introduction of a new standard of unfair trading would be a significant step forward. A general unfair practices provision would benefit consumers, business and the wider economy by improving consumer protection, increasing consumer confidence and clarifying in the law.

Consumer Action has prepared this paper to inform the upcoming review of the ACL, including the debate about unconscionable and unfair trading. Consumer Action welcomes feedback from any interested party on the directions outlined in this paper.

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