KR Hewlett and Co's

BUSINESS and EMPLOYMENT NEWSLETTER

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to the first edition of our firm's Business and Employment Newsletter. **Please feel free to start reading at any part you like**. All of Vanessa, Kim and Keith wish you well and hope you enjoy!

TRADE PRACTICES ACT

Rights that are waiting to be used when needed

The Commonwealth Trade Practices Act, and various NSW state laws too, provide business with powerful protections against misleading deceptive or unconscionable conduct. We briefly discuss them here.

UNCONSCIONABLE CONDUCT

In general, unconscionable conduct could be described as being taken advantage of in a transaction "in a way that offends the conscience."

As a more detailed general statement, we refer to the judicial endorsement of Judges of the Full Federal Court in a leading case in this area of the comment:-

> *"Four classes of case attracting the application of the language of unconscionability are described in LBC, Laws of Australia, vol 35 (at 31 January 2002) Unfair Dealing 35.5 Notion of Unconscionability [1]-[38]:*
>
> *(i) Exploitation of vulnerability or weakness*
> *(ii) Abuse of position of trust or confidence*
> *(iii) Insistence upon rights in circumstances which make that harsh or oppressive*
> *(iv) Inequitable denial of legal obligations…"*

"Traditional" unconscionability could be said to be where a person's will is so overborne by their *special* disadvantage being taken advantage of that they did not act truly independently or voluntarily.

In a commercial context however, if a commercial vulnerability of a party is no fault of the other party, that commercial disadvantage (even if very substantial) will not by itself necessarily be considered to be of *special* disadvantage.

Government laws which prohibit "traditional" unconscionability, include section 51AA Trade Practices Act.

The extended reach of subsection 51AC Trade Practices Act

Government laws go *further* to extend the power of unconscionable conduct laws to protect people in business – for example, section 51AC Trade Practices Act for "small" business transactions, section 62B Retail Leases Act (NSW) for retail leases and section 12CC ASIC Act for business financial service transactions

While those sections are similarly worded, section 51AC applies generally to transactions between businesses, but there is unusually a monetary ceiling on the transactions it will apply to – it applies to transactions of less than $3million currently (this may increase to $10million in future).

In considering the application of these types of laws, the courts will usually consider a list of factors, such as what is reasonably necessary to protect a party's legitimate interests and a party's willingness to negotiate.

 Compliance with a relevant code of conduct is another factor the court will take into account, which maybe useful in areas like the banking, franchise or real estate industries.

How far do these sections go? – some examples

 In an early case, liability was found when a franchisor was found to have refused to deliver franchise products, failed to negotiate, excluded franchisee details from advertizing, competed with franchisees and refused to provide disclosure documents. It was considered there that the behaviour was not only unreasonable, but unfair bullying and thuggish.

 In a recent case, unconscionability was found where a business supplier claimed to visit business customers to check customer satisfaction, on those visits had the business customers sign forms to "acknowledge the visits" which were in fact contracts, did not disclose terms of the contracts, later insisted on performance of the contracts, informed the business customers that they were not entitled to terminate the "contracts" and threatened legal action if the customers did not comply with the contracts.

 In one retail lease case, the use of landlord's remedies "out of commercial context" and failure to comply with industry standards was indicated to be sufficient to form the basis for a claim of unconscionable conduct.

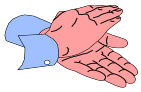
The use of landlord's remedies "out of commercial context" is expressed to indicate situations such as where a landlord may seek to suddenly strictly enforce certain lease obligations of the tenant for no apparent reason or for reasons unrelated to the clauses that landlord is really trying to enforce.

 In another recent lease case, a senior court has commented that there may be circumstances where a landlord gives a tenant an invalid relocation notice, combined with other factors, that could constitute unconscionable conduct which could give the tenant a right to damages.

Another Court of Appeal judgement however has recently stated, in general comments in a lease case, that unconscionable conduct should be a doctrine of "..application when the circumstances are *highly* unethical" (our emphasis) and should not be the "first and easiest port of call when any dispute ..arises".

Conclusion

The width of commercial unconscionable conduct laws are still being worked out, but are becoming clearer. In particular situations, provisions other than unconscionable conduct law may certainly be more applicable, but the unconscionable conduct laws should certainly be considered if a dispute arises.

 These laws have already had some effect in Australia. Commercial organizations are more willing (to some extent) to negotiate.

 If in your business legal life (or even in your personal financial or commercial legal life), an organization's or person's behaviour is heading towards being "bullying or thuggish", is unreasonable in many respects or is harsh or oppressive or highly unethical, these laws may assist.

TRADE PRACTICE ACT "MISLEADING OR DECEPTIVE" CONDUCT

Introduction

Perhaps even more powerful than the laws of unconscionable conduct are the longstanding laws prohibiting "misleading and deceptive conduct in trade or commerce – the famous section 52 Trade Practices Act, and its state law equivalents contained in the NSW Fair Trading Act and the Retail Leases Act.

 These laws make material misrepresentations unlawful, but they go further. These laws basically indicate that a business or enterprise should not, *in trade or commerce*, engage in *any* conduct that is misleading or deceptive or that is likely to mislead or deceive.

What is Trade Practice Act section 52 "misleading or deceptive conduct"?

Proof of intention to mislead or deceive is *not* generally required in order to establish a breach of the relevant laws. If the conduct misled or deceived, or is likely to, the laws maybe breached…

Statements made as to future matters that turn out later to be incorrect can also be in breach of those laws, if there were no reasonable grounds for making those statements at the time they were made.

 Even a deliberate silence where it is reasonably expected that there should be disclosure may *sometimes* be in breach of the law.

Other important matters about section 52

A wide range of remedies can be claimed for breach of section 52. To claim remedies, there must normally be *reliance* by the victim on the misleading or deceptive conduct.

 A party however cannot generally exclude liability for misleading or deceptive conduct by the inclusion in a contract of a general exclusion term. Third parties involved in a breach (perhaps such as directors of companies, agents or related parties) can also be held liable as accessories.

 Interestingly, those laws could apply to the sale of an investment property (which sale could be considered to be "in trade or commerce"). Although they usually do not apply to a private sale of a private principal place of residence, the similar unwritten law of "misrepresentation" – which is also quite far reaching - may well still apply.

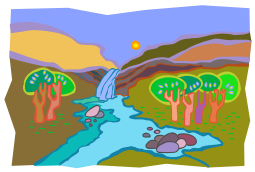
How do the section 52 laws work in practice?

A good recent example, in my view, is shown by a case relating to the combined sale of both a property and a winery type business conducted on the property.

The sale contract for the land and business just had one (out of two) of a married couple's name noted as vendor, that person was registered owner of the land, but the business being sold as well was owned by both of the couple.

During the purchase, the purchaser was apparently assisted by a viticulturist (a wine making specialist), as well as an accountant and solicitor and there was a long negotiation period.

The sales contract contained general exclusions - such as that the property was being purchased in present condition and situation, the vendor did not make any representation concerning that, no warranties were given as to carrying capacity productivity or uses of the land, purchase was subject to defects latent (hidden) and patent.



The problems…

Firstly - incorrect representations before exchange about a water flow rate of a water bore (actual flow rate much lower) - consisting of a verbal representation and incorrect statements in brochures, all confirmed by provision to the purchaser of a water bore driller's invoice (incorrect in that respect) from a few years previous.

The second problem - brochures and a verbal representation before exchange incorrectly indicated that 20 acres of the property was under vineyard grape plantation, when it was more likely about 14 to 16 acres.

The result..

The purchaser was able to claim substantial damages even though the contract tried to exclude liability. The case shows that as a general proposition, you cannot overcome specific material misrepresentations using general exclusion clauses.

The case also indicates the power of section 52 - that for breach of section 52, that it is not relevant whether or not there was an intention to mislead or deceive.

In relation the bore driller's invoice, even if it had been prepared a few years before and at the time of the sale the vendors had forgotten that there was a mistake in some of the information contained on it, the vendors were still held liable (NB – be careful to check the correctness of what you hand over).

The sale of land and business was (unusually in my view) combined in one contract. Although only one of the vendor couple was noted as vendor on the sales contract presumably as that person was the sole owner of the land, the other spouse was still held liable.

It was found that the other spouse was held liable as that person was a part owner of the business anyway, the business sale was combined with that of the land, that person was involved in the pre-contract negotiations and that person had signed the sales contract (even though not named as vendor)

The agent's liability

Finally, the agent escaped liability in this case due to factors such as that they just passed on information "for what it was worth" that they had received from the vendor, the agent indicated in their brochure disclaimer that they were just passing on information from a third party and the agent did not claim to be an expert themselves in the matters of concern. If the facts had been slightly different however, the agent would likely have been liable.

Not all cases claiming "misleading or deceptive" conduct succeed

For example, in the taking on of a retail food sale franchise, a purchaser essentially seemed to claim to have relied on misleading and deceptive conduct relating to forecast turnover and profitability and also suitability of a new shop premises found. The purchaser lost.

It seems the forecast turnover and profitability figures were one set (the least profitable set) from three sets of sample turnover figures, costs and profits in table form in a disclosure type document. There were multiple disclaimers in this document and the other documents however, and the court found no misleading or deceptive conduct.

To us, it indicates how easily in our enthusiasm, many people (including me) can see and recall a set of figures and have in mind that they are true indicators, but fail to see the more important surrounding qualifying wording and circumstances.

The other issue was the suitability of a new shop premise found for the franchisee by the franchisor. This was apparently chosen by the franchisor with care, but the main concern was that the franchisor had not explained that as the shop was in a new area, it would take several years to show its potential. The failure was not enough for the court to find misleading or deceptive conduct, particularly having regard to the many disclaimers and that the purchaser was able to obtain independent advice.

The case shows to be careful about figures in documents and that multiple disclaimers (presumably in lengthy documents) are important. The many disclaimers were relevant in this case to the issue of whether the purchaser relied on the two matters complained about.

Some lessons about misleading or deceptive conduct

People who honestly or dishonestly engage in conduct (even sometimes through silence) in trade or commerce which mislead or deceive can be found in breach.

Even before the marketing of a property, business or undertaking for sale, good legal advice should be sought about your duties of disclosure and how to deal with them. You can be liable for your agent's representations. Look carefully at the extent of an agent's indemnity on any agency agreement you sign.

If you have been wronged, you may have remedies, but these can expensive to pursue. Not all claims succeed, disclaimers are important.

You are better to properly formally question claims and independently investigate claims before the deal becomes legally binding.

BACK TO BUSINESS

Confidentiality - Before you sell a business

Before you sell a business, a prospect purchaser will likely wish to conduct "due diligence" searches and enquiries about the business. The concern for the seller is the case when a prospect purchaser later does not proceed, but has confidential information about the seller's business.

We recommend that the seller has the prospect purchaser sign a wide ranging confidentiality deed before the purchaser starts their due diligence checks.

Joint venture concerns

As you would be aware, joint ventures are not partnerships. Where partnerships are usually for the long run, so that the various partners owe each other substantial fiduciary (ie special, more onerous) obligations, joint ventures can be a group of people joining together for a short time for a one off transaction such as a property development or for a one-off short business undertaking.

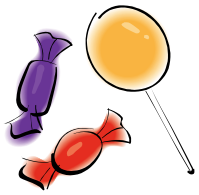
Recently, the court considered the extent to which joint venturers owed each other those fiduciary (ie special) obligations – for example, can a joint venturer withdraw from the venture and subsequently take up the same venture as their "own opportunity"?

In the case, the court seemed to have found that the fiduciary obligations of joint venturers to one another would generally not be that strong.

So, in some circumstances, parties may be able to break away from a joint venture and take their "own opportunity".

That may depend however upon the underlying contractual relationship between the parties. The case also indicated that in some situations, if a joint venturer wants to take up a similar opportunity of their own after the joint venture ends, that prior disclosure to other joint venturers (with no objection received back, or with consent received back) is at least advisable.

If you are considering entering into a joint venture of any kind, it is strongly advisable to have a proper joint venture agreement drafted clearly specifying the rights duties and obligations of the parties during the time of the agreement, and after the joint venture ends - particularly including to consider such duties as the duty of confidentiality and right of a party to take up an "opportunity of their own". Remember, if a fiduciary obligation is found, the person owing the duty may well not be able to satisfy their duty by just ending the joint venture relationship.



SHORT AND SWEET

BUSINESSES - business purchase - while section 50 of the Retail Leases Act prohibits a landlord releasing information concerning the turnover of a business of a lessee provided by the lessee, paragraph (f) of that section allows this information to be provided in good faith to a prospective purchaser of the retail shop or the building of which it forms part.

BUSINESSES - purchase - Businesses financial records - an experienced business valuer recently spoke about her experience of many years of examining financial records of businesses for sale, including those presented by Business Brokers. She indicated that her experience showed that such accounts may often be incomplete or even incorrect. Her comments are worth bearing in mind when considering the purchase of a business.

BUSINESS – What is a business worth? – The same business valuer talked about what a business is worth. She explained that many a "successful" business may offer a reasonable salary, but may cost a substantial amount of money to operate.

Apart from the (perhaps considerable) benefit of "being your own boss", a business valuer may sometimes consider that having regard to high capital outlay (and also later capital renewal costs), that a person maybe better to remain as an employee.

Whether you are looking around or already in business, it maybe useful to watch a business television show such as "My Business", read their websites or look at some trade magazines. Obviously, you should still obtain your own proper advice before starting, extending or changing a business.

CONTRACT LAW - you are usually liable for what is signed - a recent High Court case has confirmed that you are liable for what you sign.

In the case, the contract was found to include an "*Application for Credit*" form. Immediately above the place where the contract documents were to be signed were the words "please read condition of contract overleaf prior to signing". "Overleaf" (ie on the back of the form), there were about 15 conditions of the contract which were not read by the person signing the contract.

Importantly, the case also shows, as do other cases, that even if you raise a matter in writing with another party and they do not respond to that matter but overlook or ignore it, you could be liable - even if the terms of the contract you subsequently entered into are inconsistent with the matter you have raised. This particularly can be a problem where at least several matters are raised – it is easy to overlook a matter not being answered.

SECURITY INTERESTS IN GOODS ACT (NSW) 2006 - This new legislation updates the laws relating to the giving of some types of securities over some personal assets such as business equipment, and also the giving of security over animal or plant produce ("crops, stock and fish"). The new laws make it easier for financiers to lend money against such items. Please bear in mind that most (if not all) other states in Australia do not have these laws yet, so enforceability if such items can be taken interstate could be a concern.

Good legal advice should of course be obtained before borrowing or lending money against the security of such items in NSW. The NSW LPI office has now set up a security interests index that can be searched more easily for such interests registered after November 1992.

SUPERANNUATION, INVESTMENT and ECONOMICS – a recent opinion - Recently the *Sydney Morning Herald* attributed former Reserve Bank governor Ian Macfarlane opining that superannuation will now become the most important tax shelter. In his *Boyer Lectures*, Mr McFarlane also apparently proffered opinions that Australia is now without an effective economic lever to deal with what has become the biggest danger to the economy – booms and busts in the price of assets such as property and shares, that in the past, the banking sector has been shaken by recessions but that next time around the household sector could be the most vulnerable and that as a result, the downturn could be more pronounced because consumers could slash spending.

Mr McFarlane makes detailed comments about such matters and Australia's economic history since World War II as part of the 2006 Boyer Lectures. If interested, you can obtain a copy of his Lectures at the ABC Radio National website at http://www.abc.net.au/rn/boyerlectures/

TAXATION – Voluntary disclosure - It is worth considering a comment of Robert Richards, Solicitor, in a August 2005 *Law Society Journal* article:-

> "whether to make voluntary disclosure is not just problem limited to those tax payers who has been involved in offshore schemes. It is an issue that should be faced by any taxpayer who has made fictitious deductions, or who has failed to return assessable income. Taxpayers who are in such a position are often more concerned about the risk of penal prosecution than anything else. My advise to such taxpayers is normally it is better to make voluntary disclosure – while one can never guarantee it, making a full disclosure to the Tax Office is more likely to result in being more leniently treated (both as to penalties and prosecution) … if those deductions or the non-disclosure of income are subsequently discovered by, say, a Tax Office audit."

If you are considering following that guidance, you should obtain specific advice from a good lawyer or tax accountant before taking that step.

TRADE PRACTICE ACT PUBLICATION FOR SMALL BUSINESS – The ACCC website indicates that on 20 October 2006, the ACCC issued a mini-CD compilation of all their small business publications, so that small business people seeking information about their rights and obligations under the Act can find everything they need in one source. The release indicates that the compilation, called *TPA matters for small business* can be obtained free by calling ACCC Small Business Helpline on Ph 1300 302 021. We have ordered one ourselves, but the ACCC advises that our order will not be filled until late February due to updates being made having regard to recent changes to the Act.

UNLAWFUL INTERFERENCE WITH BUSINESS - This legal cause of action could possibly be considered when a person commits an unlawful act directed at another person, which interferes with that person's trade or business interest.

An article the writer has read suggests that it could also possibly apply where, for example, a competitor of your business is substantially breaching the term of their development consent to gain an unfair advantage over your business.

A High Court case confirmed a multi million dollar settlement in favour of a business where there was held to be unlawful interference with a contract. The act complained about could be an act of a competitor or even sometimes a government authority.

The width of this area of law is uncertain, unconscionable conduct maybe an alternative remedy in some situations, but there are legal principles that can be used. If such a situation arises and if there is suspected unlawful interference with your business by any person or other entity, you should obtain legal advice.

Wishing you well in business and always

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