Australian Government
Department of Industry, Innovation, Science, Research and Tertiary Education

WORKING WITH CONTRACTS

Practical assistance for small business managers

Disclaimer

This publication provides only a general outline of contract law. It is not legal advice. You should seek professional advice before taking any action based on its contents.

Internet: This Guide is available on the Department of Innovation, Industry, Science, Research and Tertiary Education's website at: www.innovation.gov.au

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What's inside …

How to quickly navigate your way through the text…

To help you find the information you are seeking quickly, these icons are used in the text.

More detailed information:

read these sections for a more detailed analysis.

Critical issue or major pitfall to avoid:

read carefully and take special note.

1 How the guide can help you

Dealing with contracts is very much a part of small business management. Once in place, contractual requirements largely dictate the way in which small businesses operate. In short, they underpin the viability and security of any business, large or small.

Confidence in working with contracts is therefore very important.

Confidence comes from understanding. This guide is specifically designed to familiarise small business managers with contracts - what they are, what they contain, how to avoid the pitfalls - and to help you get the most from these very valuable and fundamentally important business tools.

In particular, the guide provides a plain English approach to understanding:

- the essential ingredients of a contract, supported by useful and practical examples relevant to small business
- the more frequently encountered and important legal jargon used in contracts
- the different types of contracts
- the basic content and structure of contracts
- what standard form contracts are and some useful pointers on constructing your own
- some of the basic issues relating to specific types of small business relationships.

This guide also provides a summary checklist of all the issues raised and where to obtain more detailed information and assistance.

The guide is not intended to tell you everything there is to know about contract law. It will not replace the need for professional legal advice where required.

The guide is about giving small business managers the ability to be able to use contracts confidently: to be able to identify the major issues and avoid the major pitfalls.

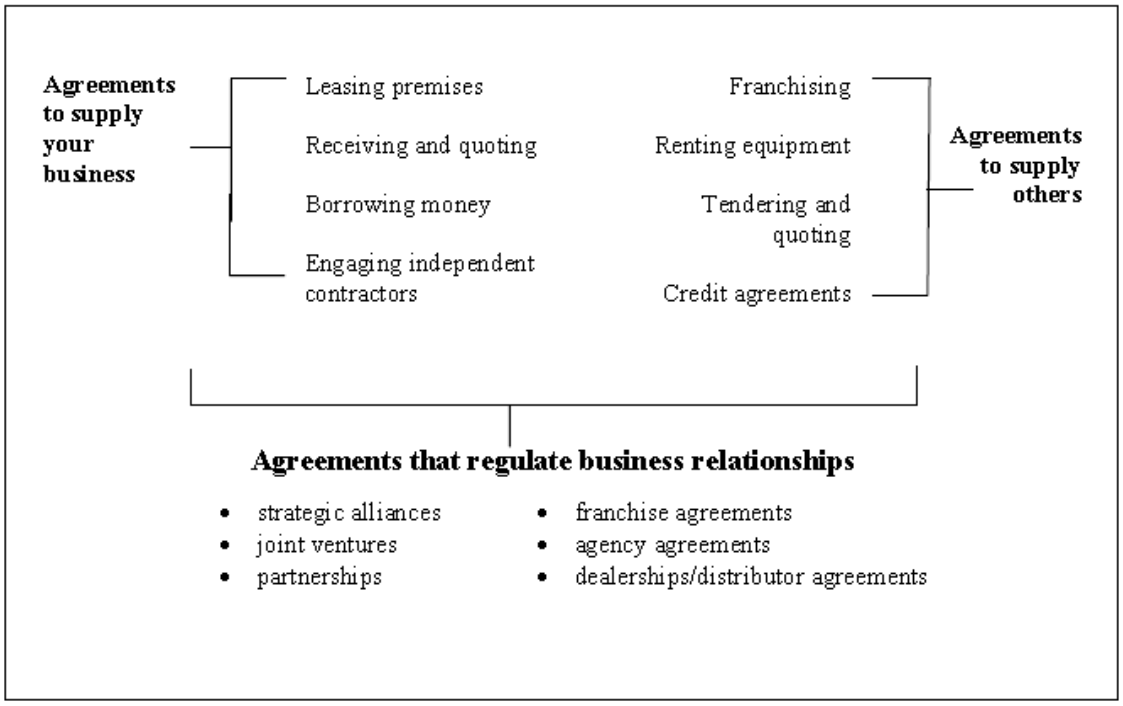
2 The 'big picture' of small business relationships

The small business sector is no different from any other sector in its need to manage a whole variety of business relationships. Most, if not all, of these relationships will involve contractual commitments and obligations. You may be:

- a consumer of goods and services - as a borrower of money, as a purchaser, in rental agreements and franchise agreements
- a provider of goods and services - retailers or independent contractors (including, professional consultants and trades people)
- in some form of partnering agreement with other businesses - *joint ventures, strategic alliances, and partnerships.*

Contracts need to be managed. It is often a good idea to keep in touch with the other party to ensure that contractual obligations are being met as they should be. Sometimes a little give and take is necessary to cope with unforeseen circumstances. Managing the relationship may be as important as managing the contract.

Managing small business contractual relationships



3 The essential ingredients of a contract

In the small business environment, discussions, negotiations and deal-making are an everyday occurrence. Typically they involve: providing quotes; discussions with suppliers, sales representatives, agents and clients; and making offers and submitting tenders.

Out of these deals, agreements are made, where someone has agreed to do something for payment. Some agreements will be more important than others, but they are still agreements.

Contracts are 'legally binding' agreements, that is, agreements which in the eyes of the law are valid and which, with certain exceptions, must be fulfilled and complied with. The question is, when does all the discussion and negotiation become an agreement, and then, when does an agreement become, in the eyes of the law, legally binding?

For an agreement to be regarded as legally binding, it must contain four essential ingredients, if any one of them is absent the agreement will not be legally binding.

The **four** essential ingredients are:

- offer
- acceptance
- intention of legal consequences AND
- consideration

'Offer'

There must be an offer to do something. The offer must be quite clearly stated, and definite in its intention.

- 'Offers' can be withdrawn at any time before they are 'accepted', unless it is a standing offer fixed for a period of time.
- There is a very important difference between an 'offer' and something simply intended to get negotiations under way. The latter are termed 'invitations to treat' and are not legally binding.

Examples

- What is likely to be an offer?
  - tender submissions
  - formal quotations
  - proposals to lease.
- What is likely **not** to be an offer?
  - 'ball park' estimates
  - advertisements
  - requests for proposals
  - expressions of interest
  - letters of intent.

'Acceptance'

The offer, exactly as given, must be clearly understood and its acceptance must be definite.

  - Only what is offered can be accepted. If any new terms are suggested this is regarded only as a counter offer which can be accepted or rejected.
- Counter offers are regarded under contract law as removing the original offer made.
- Requests for further detail about an offer are not counter offers.
- Where acceptance is given with conditions, the acceptance is not complete until the conditions are fulfilled - these are regarded as conditional contracts.

Examples

- Acceptance can be given:
  - verbally or
  - in writing
  - by an action that clearly indicates acceptance.
- Acceptance cannot be presumed through inaction or lack of response.
- You cannot say that 'I will assume you have accepted if I do not hear from you within three days'. Acceptance requires a positive action: one of the three forms noted above.
- Acceptance by mail may be considered complete at the time of posting - if this is the expected way of replying. Sometimes a letter must be received, eg insurance acceptance.
- Acceptance by electronic means, such as email or fax, is completed at the time of receipt.

‘Intention of legal consequences’

The parties to the agreement must understand that the agreement can be enforced by law.

- For a contract to be binding, it does not have to expressly state that you understand and intend legal consequences to follow.
- For commercial contracts your intentions are presumed, for example, to be legally bound.
- The parties to a contract can decide not to be legally bound by the agreement - this must be clearly stated and is then an agreement that is not legally enforceable.

Examples

- Given that your intention may be presumed, it must be made absolutely clear if you do not intend your agreement to be a legally binding agreement.

‘Consideration’

Being a business arrangement, the promise must involve giving something in exchange for something of value (the ‘consideration’). Usually the consideration involves the payment of money.

- Usually consideration is the payment, or promised payment, of money - but it can be anything of value; even items of the smallest value are good consideration.
- The payment need not be fair value for the promise.
- Consideration can also be the promise not to do something, to refrain from exercising some right.

Examples

- Consideration may be either:
- the agreed price, or
- a price which is able to be calculated.

4 More on ‘offer’: the lead up to the contract

What is actually said or claimed in marketing material, sales presentations, brochures and product specifications materials, by whom and when, during the negotiating period leading up to formalising a contract - referred to in law as ‘representations’ - can be of critical importance in determining:

- whether an ‘offer’ was actually made, as opposed to an ‘invitation to treat’, and therefore, whether a contract actually exists
- what was actually offered and accepted - the actual enforceable terms of the contract
- whether what was said, which directly led to an agreement being reached, was false or misleading to the point where any contract is made invalid.

Common law (ie law made by Judges) is not the only law governing contracts. Legislation such as the Australian Consumer Law (which is part of the Competition and Consumer Act 2010) and the State and Territory legislation on Sale of Goods or Contracts Review may also regulate the contractual relationship.

Enforceable terms

Claims or representations are the verbal and written statements made in the lead-up period which are designed to inform or persuade another party to enter into a contract. Representations include advertisements, sales pitches, and any other statements made prior to a formal agreement being made.

Representations are extremely important because they may become enforceable terms of a contract if a party has relied on them.

Therefore, written contracts should make very clear which prior representations, if any, will form part of the agreement.

If a verbal or written representation conflicts with a subsequent written contract, the terms of the written contract will generally be those which will be enforced. Generally speaking, a written contract, once signed, is difficult to terminate.

Make sure that what was claimed, either verbally or in writing, and relied upon, is clearly incorporated in the written contract

Even when the contract is wholly or partly verbal, proving that such representations have been made and relied upon can be a difficult task. Generally, in assessing the level of influence of representations, courts will consider:

- the significance of what was actually claimed
- how close to the finalising of the agreement the representations were made
- whether they convinced a person to enter the contract
- the expertise of the person giving opinions.

The representation is probably not part of the contract if it can be proven that:

- the person made up their own mind, despite what has been said, or
- it was only one of many statements made during the early negotiation stages.

Validity of the contract

The validity of the contract is determined by the manner in which a sale takes place, by what is said or not said.

Dishonest or careless statements made during the lead-up to a contract, or a person being improperly induced into a contract because of their ability in a certain language, their age or personality characteristics, may lead to parts of the contract (or in an extreme case, the whole contract) being unenforceable.

Anti-competitive agreements between competitors

The Competition and Consumer Act prohibits some anti-competitive "contracts, arrangements or understandings" between competitors, as well as some other anti-competitive activities. Many types of anti-competitive activities are prohibited regardless of how effective they are or how long they last.

Substantial penalties can be imposed for breaching the prohibitions against anti-competitive contracts, arrangements or understandings, including **significant fines** and **imprisonment**.

Great care is needed before you reach agreement, or come to an arrangement or understanding, with a competitor (whether individually or as part of a group of competitors - for example, a trade association). If in doubt, seek legal advice.

The term "contract, arrangement or understanding" is very broad and may include:

- written contracts
- a verbal agreement, or
- a "nod and a wink" arrangement or an understanding that competitors will behave in a certain way.

Who is a "competitor"?

- actual competitors - for example, other businesses which currently offer similar goods or services as your business, and
- potential competitors - for example, businesses that would be a competitor if an anti-competitive contract, arrangement or understanding was not in place.

The main types of prohibited activities are contracts, arrangements or understandings where competitors agree to:

- **fix prices** - for example, by agreeing the price they will charge customers, the discount they will give, or that they will not lower their prices
- **share markets** - for example, by dividing up a market in terms of products they will sell, customers they will serve and the geographic markets within which they will operate
- **rig bids** - for example, by deciding that company A will submit a higher tender price or a non-conforming response so that company B has a greater chance of winning the tender
- **prevent supply or restrict outputs** - for example, by agreeing that one or more of the parties will restrict the amount of goods they produce or their capacity to provide services, or that the parties will not supply certain persons or groups of persons (including other businesses)
- **resale price maintenance** - for example, where a supplier sells to a business on condition that the business does not resell the goods below a specified price, or the supplier withholds supply because a business has not agreed to resell above a minimum price ("recommended retail prices" are acceptable provided the purchaser is genuinely free to set their own resale price)
- **third-line forcing** - for example, where a supplier:
  - sells on condition that the purchaser is required to obtain other goods or services from a specified third party, or
  - refuses to sell because the purchaser has not obtained other goods or services from a third party.

The activities on page 8 are some of the main anti-competitive activities that are prohibited under the Competition and Consumer Act. There are other prohibitions. If in doubt, seek legal advice before entering into any contract, especially where you are dealing with a competitor or you are restricting one or more of the parties' ability to price goods or services.

There are a number of exceptions to the prohibitions outlined above. For example, where competitors are entering into a joint venture or where related bodies corporate are contracting with each other. However, these exceptions often give limited protection. You should seek legal advice before relying on any exception.

In some cases, it is also possible to seek "authorisation" from the Australian Competition and Consumer Commission (ACCC) for anti-competitive arrangements or conduct. Before it grants authorisation, the ACCC must be satisfied that the public benefit of the arrangement or conduct outweighs any public detriment. Authorisation provides immunity from legal action under the Competition and Consumer Act.

Case Study

At a recent industry lunch for soft drink retailers, a representative of one company mentioned to a competitor that it would be lowering its lemonade price to $1 for a short period of time. As it turns out, each of the other retailers in Canberra followed suit. After two weeks of lemonade prices at $1, another retailer contacted a competitor and said that it would raise its prices to $2 the following week. Soon, the price of bottles of lemonade in Canberra increased to $2. This process took place a number of times in the following months.

In this scenario, although there appears to be no formal agreement between the lemonade retailers to set the same price, the courts could interpret the discussions between the retailers to be an anti-competitive arrangement or understanding. A court would consider whether there is a an agreed approach to setting prices between the retailers. In this situation, it might be that each retailer spoke to the other and undertook to increase or discount only after talking with the other retailers. Conduct is not necessarily anti-competitive merely because the price of lemonade is the same across the retailers. If there were no discussions between the retailers and they had each made an independent decision to raise the price of their lemonade after having seen the other retailers' conduct, then this is unlikely to be an anti-competitive 'arrangement'.

The Australian Consumer Law applies to all businesses, including companies and sole traders. It prohibits misleading or deceptive behaviour when making a contract.

Advertising

Generally, while it is acceptable to give full praise to your product/service, it is against the law to make claims that are misleading or deceptive.

In this situation, the actual words used in the advertisement are all important. Avoid concrete promises that you know are untrue. Exaggeration that is merely descriptive, and obvious as such to the reader, may be acceptable (called 'mere puffery' at law).

The overall impression given must also be correct. For example, it is a breach of the law to give people the impression that everything is 50% off, even if you state in the fine print that this only applies to clothing and footwear.

Avoid claims that compare your services to others. For example, claiming that you are the "best in town" may constitute a breach of the Australian Consumer Law.

Opinion

It is perfectly acceptable to give an opinion, which may be acted upon by the customer, as long as you honestly believe the opinion is true.

If customers act on opinions which are false, those providing the opinions may have broken the law if the opinion:

- made it reasonable to expect that people would act upon the false impressions given; or
- is known to be false by the person giving it; or
- falsely conveys the impression that it is the opinion of an expert.

Truthful impressions

Holding back important information, which may lead to false impressions about important aspects of the good or service, can be unlawful.

Pressure tactics

Putting pressure on someone to 'close a deal', by making false claims concerning product shortages and deadlines, may be an unlawful practice. All claims must be correct and convey the full picture.

The law also looks unfavourably on some tactics designed to force parties into contractual arrangements. This can happen when a company is in a very strong bargaining position and attempts to use its advantage to force weaker parties into accepting unnecessarily harsh or unfair terms.

5 The different types of contracts

With certain specific exceptions, contracts do not have to be in writing to be legally binding.

However, signed written contracts are usually the most desirable form of contract, especially when it comes to business arrangements. After all:

- the contents ('terms') are in writing for all to see
- they can ensure that precise language is used in describing the terms of the agreement
- there is, therefore, less opportunity for misunderstandings and conflicting assumptions
- there is less need to rely on memories of what was originally agreed
- the individuals involved in the transaction may change over time.

In fact, the law recognises a number of different types of legally binding contracts:

Written	**Verbal**	**Mixture**
• Formally agreed • Standard form • Simply a letter confirming an agreement	• Verbal agreements can be just as binding as written agreements	• Contracts can be a mixture of verbal and written terms

Verbal agreements may be difficult to prove, difficult to remember precisely, and open to misunderstanding. In resolving a dispute on this issue, the conduct and statements made by each party leading up to the contract under challenge will be the critical issue.

In business arrangements, it is usually preferable to have all terms of the agreement in writing in order to avoid the problems of:

- proving a contract existed
- proving it to be a complete or incomplete document
- proving verbal undertakings
- interpreting people's conduct.

Summary of important issues

Written contracts

- When a contract is signed, it is generally assumed that all the terms have been read and agreed to.
- If unsigned, a written contract must:

- be presented to and understood by all parties to be valid before the transaction occurs, and
- be recognised by all parties as a contract, that is, it must look like a contract and not simply a receipt or docket.

Clearly, unsigned contracts may be more difficult to enforce.

Verbal agreements

- Verbal agreements rely on the good faith of all the parties and can be difficult to prove.
- Conversely, in some situations, insisting on a detailed written agreement may be counter-productive if:

- the value of the transaction is not particularly high, and/or
- the presentation of a substantial document, possibly with many provisions, may raise more questions and uncertainty in the minds of the parties than it resolves, ending in the transaction not proceeding. If you are confident of the good faith of the party, a shorter form of written arrangement may be the best course of action.
    - Do not automatically think that because it is not in writing, it can never be proved. Verbal agreements can be supported by:
- the conduct of the other party both before and after the agreement
- specific actions of the other party
- past dealings with the other party.

Case Study

Sarah entered into a written contract with Mary's Design Company to hire the Company as her graphic designer for two years. The contract gave Sarah an option to renew the contract at the end of the two years. Sarah liked the Company's work so much that she tried to exercise the option. However, Mary told Sarah that Mary's company was only looking for larger contracts now and did not want small contracts such as Sarah's anymore. Mary pointed out that when Sarah first met Mary, Sarah had promised Mary a large amount of work and that Sarah had failed to that level. Sarah disagrees with Mary.

As the dispute concerns a potential verbal term of a contract, a court would need to decide, on the basis of the evidence, whether Sarah or Mary's claims as to what took place is what was actually agreed between them. The actions and statements of the parties is crucial and other witnesses to the meeting may be critical in proving the claim of one of the parties. It is possible that a breach of the verbal agreement regarding the amount of work that Sarah would give Mary's Company means that Sarah is not able to exercise the option to renew. However, the the verbal term of the agreement may be difficult to prove and will depend on the reliability and memory of the witnesses.

6 Contracts: what's in them

Although contracts vary in complexity, they all have a similar basic content and structure.

The whole point of a contract is to spell out as clearly as possible what are the agreed obligations of each party, what payment or other 'consideration' is involved, and any other terms relevant to the specific circumstances.

Good contracts are those where the parties have carefully considered all the circumstances that are likely to arise during the lifetime of the agreement and have adequately provided for them. Such contracts will have clearly and fully covered such matters as:

- exactly what is required by each party
- limits to what is required
- payment terms, including credit terms and under what circumstances
- risk: what could go wrong in the relationship and how to provide safeguards against this.

Terms of a contract - express and implied

The terms of a contract are all the points of agreement between the parties concerning just how and under what circumstances the agreement is to be fulfilled. With some clear exceptions noted below, contract law does not specify what those terms must be: they are up to the parties to determine.

Contract law recognises two types of terms: *express* terms and *implied* terms.

Express terms

These are the terms of the contract which are specifically agreed to between the parties and are put in writing in the contract or agreed to verbally between the parties.

Implied terms

Some terms may not actually be put in writing, talked about or even considered - but they may be implied into the agreement and are binding nevertheless.

These terms may be implied because the law requires them to be part of the contract, or because common sense, standard industry practice or past dealings create a reasonable expectation about how the agreement will be carried out and to what standard.

Considerable care needs to be taken on this issue of implied terms. If the terms of the contract are going to be carried out differently from what would normally be expected by common sense, standard industry practice or past dealings, they must be clearly stated in the contract.

Implied terms

- **Common sense:** In an agreement there may be some matters which are implied because they are so obvious that they go without saying. For example, common sense dictates that goods are appropriately packaged.
- **Standard commercial practice:** Each industry, unless the agreement involves an entirely new product or concept, will have well established customary practices, including recognised quality standards and terminology. They may be implied in your contract.
- **Past performance:** Past dealings and arrangements create an expectation that future agreements will be carried out in the same way, unless the parties decide to change the arrangement. Again, past performance may be the benchmark for future contracts. If you want otherwise, the contract should say so as part of its express terms.
- **The law:** The Australian Consumer Law contains a number of "consumer guarantees". While these guarantees are not implied into contracts, they do create a basic set of protections for consumers who acquire goods or services, so you need to be aware of them when entering into consumer contracts (generally contracts where the amount payable is $40,000 or less, or the goods or services are of a kind ordinarily acquired for personal, domestic or household use). You cannot contractually exclude the consumer guarantees, but in some cases you can limit your liability. Consumer guarantees include a guarantee that:
  - the supplier has the right to sell the goods to the consumer
  - the goods are of an "acceptable quality" - for example, they are free from defects and are safe
  - the manufacturer will comply with any express warranty given
  - services will be provided with due care and skill and within a reasonable time.

State and Territory Sale of Goods Acts may also imply some important terms in non-consumer contracts for goods:

- goods and services sold must be of a good (merchantable) condition
- a sample shown to the buyer must be the same as the bulk of goods
- the goods have been correctly described, by the seller or their packaging
- the holder of the goods has the right (title) to sell the goods
- the goods will be fit for any purpose made known to the seller.

Implied Terms

Case Study

Dryclean UK operates a chain of drycleaning shops in the UK. A few years ago, it entered into an arrangement with Mean Clean, an Australian company, allowing Mean Clean the right to develop the Dryclean UK franchise in Australia. The contract required Mean Clean to open 5 new outlets every year with the approval of Dryclean UK. Last year, Dryclean UK decided that it wanted to start its franchise in Australia directly rather than through Mean Clean. It began secretly talking to other companies to open Dryclean UK outlets and withheld its approval for Mean Clean to open any new outlets. The contract does not expressly say that Dryclean UK cannot do this. Dryclean UK decides to terminate the contract. Mean Clean then decides to sue Dryclean UK for a breach of an implied term in the contract that the parties act in good faith.

Contracts may contain both express and implied terms. An implied term of good faith is generally considered to apply to most contracts. In this example, the withholding of approval for the opening of new outlets is likely to be a breach of the implied term of good faith in the contract between Dryclean UK and Mean Clean.

Major and minor terms: conditions and warranties

In contract law, the terms of a contract, whether express or implied, have different levels of importance.

In viewing all the agreed terms as a package, contract law is very careful to distinguish between those terms, whether they be express or implied, which will be regarded as "**contract conditions**" (major terms) and those which will be regarded as "**contract warranties**" (minor terms).

Contract conditions

Contract conditions go to the very heart of the agreement. They spell out what is absolutely fundamental to it, and if not fulfilled, will make the agreement pointless. For example, a printer orders a printing press but receives a refrigerator; products arrive too late to be exhibited; a franchisor fails to provide marketing support for a franchisee.

It is therefore essential that in negotiating contract terms you:

- decide what will be the conditions of the contract
- ensure that you have agreement from the other party on these conditions
- check that the contract makes clear what these conditions are.

Contract warranties

Contract warranties are terms of lesser importance and are not fundamental to the contract.

The distinction between these two types of terms is critical. Failing to comply with contract conditions may result in the contract being terminated and compensation being payable to the other party for loss or damage that resulted from non-compliance.

A breach of warranty will not lead to termination but may involve compensation.

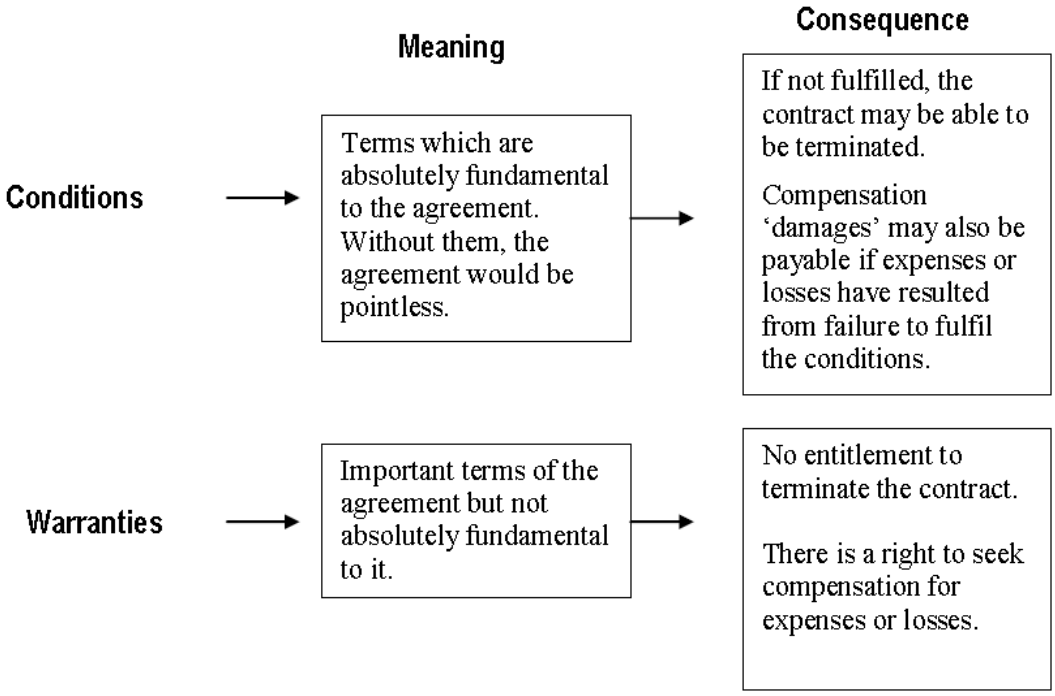
Case Study

Bob, an independent contractor, was contracted by Janet at AussieMag, a local NSWmagazine company, six months ago. A clause in his contract required him to prepare a monthly fashion section for the magazine. The contract also says that Bob's fashion section would be given at least 5 pages of the magazine with photos and a story as a major feature at the front of the magazine. Bob had a number of other offers at the time but he chose AussieMag. He told Janet that he was very excited as he had always wanted a major feature in a magazine to showcase his work and this had convinced him to contract with AussieMag.

Bob's section has now been moved to the back of the magazine and given only half a page to make room for a new feature on interior design. Bob told Janet that AussieMag had breached a condition of his contract and he was no longer bound by the contract and would be writing for a local newspaper instead. Janet responded to Bob saying that the location of his article in the magazine and how many pages he was given was not an important part of the contract.

Bob's contract does not use the language of "condition" or "warranty". However, the clause requiring him to prepare his monthly fashion section would clearly be a condition given that it is fundamental to the contract. The question is whether the clause regarding the number of pages and location of Bob's article is a condition, a breach of which allows Bob to terminate the contract. The courts will generally consider the particular circumstances and look to decide whether Bob and Janet intended that particular clause to be that important.

Contract terms



- It is important to make sure that if a term has not been carried out, it is correctly identified as a condition or warranty. A person risks being sued for non-performance if they improperly terminate a contract because a warranty was not satisfied.
- Circumstances will determine whether a particular requirement is a condition or warranty. A term may be a warranty in one instance and a condition in another. For example, if timeliness in delivery is critical, it may be a condition; if merely desirable, it may be a warranty.

Typical content and structure

Before peering into the fine print, you should be clear about what you and the other party expect from the contract. Your expectations may be simple, immediate and strictly commercial, or they may be longer-term, less immediately focused on achieving financial returns and more strategic in their objectives. Whichever is the case, it is essential that you all agree on what the contract is expected to deliver.

When overall objectives are clear, navigating your way through the contract can be a much easier task. Remember, all contracts have a basic content and structure.

The following pages outline some of the more fundamental issues to consider when entering into contracts and how they are typically covered.

Overall objective ...

- what do you and the other party expect from the relationship?
- critical starting point for assessing contract content.

Typical content and structure ...

what is agreed, for how much, and under what terms such as:

- who are you dealing with?
- what is involved?
- the meaning of key words
- risk management issues
- contract performance
- dealing with difficulties and changed circumstances.

Goods and Services Tax

You should be aware that the majority of contracts entered into will have Goods and Services Tax (GST) implications.

Issue	Relevant contract term	What is covered in a contract
Who are you dealing with?	'contracting parties'	The very beginning of the contract will outline the exact identity, including address, of each of the parties. The contracting parties may be different from the people you have been negotiating with. Only those parties to the agreement are responsible for it.
	'team members'	If a team of individuals is involved, parties may wish to ensure that specific individuals, and they alone, are responsible for fulfilling the agreement. In this case the contract should specify their identity and provide for the conditions under which they may be replaced.
	'subcontracting' and 'assignment'	If relevant, the contract will specify whether any form of subcontracting is permissible and if so, under what conditions. Assignment provisions will indicate under what circumstances, if any, the benefit of the contract can be assigned to third party.
What is involved?	'purpose'	The contract will specify the nature of the agreement being entered into, what is to be done by whom and any limitations to that.
	'payment'	The terms, timing and method of payment should be clearly identified.
The meaning of key words	'interpretation'	The agreement will use key words to describe trade jargon, relevant commercial practices, production processes to be used, delivery modes etc. The exact meaning of these words is critical to successfully fulfilling the contract and needs to be defined at an early stage in the document.
Risk management issues	'default'	A contract may state that it must be performed in a certain way or meet progressive deadlines: examples might be a payment of interest, or works completed. If a payment deadline or some other stipulation is missed, this may be a default and may lead to the cancellation of the contract. Note that courts do not always enforce these where they believe them to be unreasonable in the circumstances.
	'indemnity'	The contract may provide an indemnity clause which generally seeks compensation from one party to the agreement for liability incurred by the other.
	'exclusion'	Exclusions and exemption clauses seek to exclude, limit or cap liability in specific circumstances. Commonwealth and State legislation will overrule some exclusion terms.
	'director's guarantee'	A supplier or lender to the business may require that a director personally guarantee any debt incurred by their business. If the business is unable to meet its obligation, the director will be personally liable.

Issue	Relevant contract term	What is covered in a contract
Contract performance	'bonus' and 'penalty' provisions	A contractor or an employee may receive an extra payment or a share of profits from a project if a contract is completed at a higher than stipulated quality, or before a maximum time set in a contract. A penalty may apply in the case of late or incomplete performance.
	'completion'	The contract should make clear exactly what constitutes satisfactory completion of the contract.
Dealing with difficulties and changed circumstances	'renegotiation'	A contract can always be amended by agreement. Something may happen during the life of the contract which affects the ability of one or more parties to perform the contract. To provide for this possibility, the contract should specify the conditions under which renegotiation is permissible. It may be that a new contract results or that the existing contract is amended and remains in force.
	'dispute resolution'	Disputes arising during the life of a contract may be settled by the parties themselves, or ultimately by a court or tribunal. Some contracts now have terms which require the parties to first negotiate between themselves or use a mediator or an arbitration process before going to court, as a less expensive way of settling a dispute.
	'termination'	The contract should state under what circumstances the agreement can be terminated, and what financial obligations/compensation must be settled, if any, as a consequence of termination.

7 Standard form contracts

What is a standard form contract?

Standard form contracts are pre-prepared where all the legal terms have already been set. You may experience such contracts:

- as a recipient of a standard form contract, where there is little or no prior negotiation. The contracts are normally printed so that there are only a few blank spaces left to fill in, such as names and signatures, or
- as a provider of a standard form contract, in which you have your own standard terms and conditions.

Standard contracts may contain a multitude of terms and be pages long, or can be straightforward documents which are simply designed to name the parties to an agreement along with dates, subject matter and any special requirements.

Important features of standard form contracts are that they are:

- usually written in favour of the party presenting them
- often used by large corporations, including financial institutions, which have many clients, and are typically presented for contracts involving insurance, leases and mortgages - but they are also used by the full range of business organisations
- often used as an attempt to limit liability for damages, losses or delays by the party presenting the standard form agreement, who is usually the bigger and stronger party in the contract.

Once a standard form contract is signed or accepted it is presumed to have been read and agreed to. Standard form contracts are often printed on the back of a standard business document - order forms, invoices, quotations, delivery documents - usually in fine print. They can be just as binding as a fully negotiated contract.

Consumer contracts and unfair terms

Under the Australian Consumer Law, unfair contract terms in standard-form consumer contracts are void.

A contract term will be unfair when it:

- causes a significant imbalance between the parties under the contract
- is not reasonably necessary to protect the interests of the supplier, and
- it causes a financial or non-financial detriment to a party.

The prohibition against unfair terms only applies to "consumer contracts" with natural persons. That is, to contracts:

- for the supply of goods or services, or
- the sale or grant of an interest in land, where the acquisition of the goods, services or interest is predominantly or wholly for personal, domestic or household use.

The law against unfair terms does not apply to all terms in a standard-form contract. The law does not apply to:

- terms that define the main subject matter of the contract - for example, a customer cannot claim that a term is unfair because they have changed their mind about the good or service they agreed to buy,
- terms that set the up-front price to be paid under the contract, and
- terms allowed or required by another law.

Important issues

- There is nothing stopping you from attempting to renegotiate the terms of the contract.
- Any changes to the terms must be presented to the other party and agreed to before the contract comes into existence.
- Even if the contract does contain an unfair term, you may still be bound by the rest of the contract, if the contract can operate without the unfair term.
- The other party to the agreement must be aware that it is of a contractual nature and contains terms. If it is just a receipt, docket or a sheet of information and not expected to contain a legally binding agreement, the terms may not be enforceable.
- The terms of a standard form contract cannot override consumer guarantees and some terms implied by legislation.

'Battle of the forms'

Where the parties negotiating an agreement each have their own standard form contract - and these are exchanged - there may be a presumption in law that the last form presented takes precedence. You should therefore be careful in accepting another contractor's documentation - and their terms. It may be more prudent to construct a mutual contract.

Constructing your own standard form contract

For small businesses which engage in a number of essentially identical contracts, it may be worthwhile having your own standard form contract which sets out the terms and conditions either for the acquisition or provision of goods and services.

- When buying goods or services the standard form contract can be printed on, or sent with, the order form.
- When selling goods or services the standard form contract can be printed on, or accompany, the quotation or proposal.

The exact content and structure of your standard form contract will depend entirely on the nature and complexity of the business you are in.

The prohibition against unfair contract terms also applies to small businesses. You must not include any unfair terms in your own standard form contracts. You need to consider whether each clause is reasonably necessary and whether it will not disadvantage your customer without good reason.

Seeking professional advice may be a sensible precaution to ensure the terms cover your particular requirements and address important issues which might not have occurred to you. However, you can certainly limit your exposure to legal costs and ensure the terms and conditions meet your requirements by considering some fundamental issues.

Useful pointers in constructing your own standard form contract

When constructing your own standard form contract it is a sensible option to consider whether the contract:

- clearly and completely identifies what goods or services are being provided or obtained so that there is no room for ambiguity
- (where your customers are individuals and not a business) has any terms which:
  - would result in a significant imbalance of the parties rights and obligations
  - are not necessary to protect your rights
  - might cause you customer detriment if you relied on the term
- clearly identifies what will be required to successfully fulfil or complete the contract, including a clear indication of contract conditions, such as:
  - required quality and any tests that are to be satisfied
  - timeliness of delivery or other relevant milestones
  - time and method of payment
  - warranties and other support services
- clearly identifies any special arrangements which you require that may be contrary to standard industry practice or which differ from past practice
- minimises your exposure to possible risks. This might be by limiting or capping your liability to the minimum legal requirements and maximising the potential liability for default of the other party (note that liability caps only limit your liability to the other party to the contract - they do not protect you from liability to anyone else)
- ensures that there are suitable mechanisms for resolving disputes in a timely and cost-effective manner
- ensures that there are suitable mechanisms for varying the contract so that both parties understand any changes to the price, delivery times or other relevant terms. Unilateral rights to vary standard form consumer contracts may be unfair (and therefore void) unless customers have a right to terminate the contract without penalty should the terms be varied
- provides a clear statement of how the contract can be terminated in the event of default or other specified events and what is then to be done by the parties
- avoids using complex or overly technical language when drafting standard form consumer contracts. Terms which are unclear are more likely to be considered unfair.
- protects confidential information and intellectual property rights.

Things to look out for in standard form contracts

Examples in finance contracts

- Contracts that provide credit for a purchase are specifically regulated by the National Consumer Credit Protection Act, the National Credit Code and the Australian Consumer Law. Therefore, the information required to be provided is quite specific. Each contract must contain information about:
  - the credit provider's name
  - the amount of credit
  - interest rates
  - repayments
  - fees and charges
  - pre-contractual information that must be supplied
  - other information set out in the legislation.
- Any standard form finance contract which does not comply with these legal requirements may be invalid.
- If you are providing credit, then you may be required to hold an Australian Credit Licence and you should seek professional legal advice.
- For further advice and assistance, contact the Financial Ombudsman Service, telephone 1300 780 808, or www.fos.org.au, or the Australian Securities & Investments Commission, telephone 1300 300 630, or www.asic.gov.au.

Examples in insurance contracts

- Insurance contracts may contain numerous industry specific terms, exemptions and limiting clauses.
- The liability of insurers usually hinges on the meaning of key words and how the insurance company will choose to interpret them. They require careful examination of terms such as:
  - expiry date
  - items/services insured
  - limits to insurance cover
  - what is not insured
- These contracts may also refer to documents and rules outside the contract, such as the General Insurance Code of Practice.
- A feature of standard form insurance agreements is the need for those seeking insurance to provide 'utmost good faith'. Failure to honestly and fully disclose required information, depending on its significance, could invalidate the contract.
- For further advice and assistance, contact the Insurance Ombudsman Service which is now part of the Financial Ombudsman on telephone 1300 780 808, or www.fos.org.com.au.

The Insurance Ombudsman Service will assist consumers and small businesses with an annual turnover of less than $1 million. The businesses must be independently owned and operated and the service only relates to certain insurance policies.

Examples in retail tenancy contracts and commercial leasing contracts

- A non-residential lease is often used as an example of the potential inequality of parties, especially where the owner of the premises is a large corporation which owns and manages a large office block or a large retail precinct in a popular location. A small business in taking a lease may be presented with a document specifying a number of obligations and fees, but often with minimal requirements on behalf of the owner of the premises.
- State/Territory retail tenancies legislation, which considers small businesses, provides some protection.
- The decision to sign or not sign the lease should be an 'on balance' decision, based on the important legal and commercial considerations involved in the deal.
- Consider carefully the issues of:
  - location
  - rent increases
  - fit-out and other costs
  - the bond
  - lease renewal
  - termination.

The following State and Territory agencies may be able to provide further advice and assistance relating specifically to your business's contracts:

ACT Office of Regulatory Services

phone (02) 6207 3000 or email ors@act.gov.au

http://www.ors.act.gov.au/

NSW Office of the Small Business Commissioner

Phone 1300 795 534 or email we.assist@smallbusiness.nsw.gov.au

www.smallbusiness.nsw.gov.au

Vic Office of the Small Business Commissioner

Phone (03) 9651 9316 or email sbc@sbc.vic.gov.au

www.sbc.vic.gov.au

Tas Consumer Affairs and Fair Trading

Phone 1300 654 499 or email consumer.affair@justice.tas.gov.au

www.consumer.tas.gov.au

SA Office of the Small Business Commissioner

Phone (08) 8303 2026 or email sasbc@sa.gov.au

www.sasbc.sa.gov.au

WA Small Business Development Corporation

Phone 131 249 or email info@smallbusiness.wa.gov.au

www.smallbusiness.wa.gov.au

Qld Queensland Government Business

Phone 13 74 68 or email government.gateway@qld.gov.au

www.business.qld.gov.au

NT Department of Business and Employment

Phone 1800 193 111 or email territory.businesscentre@nt.gov.au

http://www.nt.gov.au/dbe/

8 Specific small business relationships

Contracts which are specially designed to establish the agreed ‘rules’ for substantial long-term business relationships need to be quite specific and thorough in their treatment of a number of key issues:

- the rights of the parties involved - who will receive what?
- the duties of the parties involved - who must do what in return?
- any limits to these rights or duties
- how to anticipate any difficulties.

Agency, franchise and partnership agreements are some of the most common small business relationships.

The following is a guide to some of the more important issues which each contract should address.

Partnership agreements

Definition

A partnership is a combination of two or more persons who conduct a business together and share the profits, noting that under the law the word ‘person’ can also mean an organisation.

Apart from specific partnership agreements, there are a variety of other relationships involving some form of partnering with other businesses, including:

- joint ventures
- strategic alliances
- consortia
- teaming

What if there is no written partnership agreement?

In the absence of an agreement between partners, partnership law may impose specific requirements on the partnership, including:

- a statutory interest rate on lending by a partner to the business
- an equal share in the partnership for every partner
- equal management powers for each partner
- a duty to be honest and accountable to the partnership, which itself imposes a number of requirements on the behaviour of each partner.

Issues a partnering agreement should cover

- Will some partners have greater responsibilities than others, for example, a senior partner or managing partner?
- If so, what will their individual rights/responsibilities be?
- Will some partners contribute more money to the business than others?
- If so, what will their individual rights/responsibilities be?
- How does an existing partner leave the relationship?
- What happens if more money is required to be contributed?
- How are decisions made in the relationship?
- How will profits be distributed?
- How can the relationship be wound up?
- Is provision to be made for the spouse/children of a deceased partner?
- Is it clearly stated between the parties as to their agreed liability, for example, is it a formal limited liability partnership or are partners jointly and severally liable?

Franchise agreements

Definition

A franchise agreement is a contract in which the franchisor grants to a franchisee, for a fee, the right to carry on a business of supplying goods or services under a system or marketing plan that is associated with a trademark or advertising symbol owned or specified by the franchisor.

The Franchising Code of Conduct

Franchises are regulated by the Franchising Code of Conduct, a mandatory code under Competition and Consumer Act. The Code requires, the franchisor to provide a prospective franchisee with a copy of the franchise agreement, in the form in which it is to be executed. Additionally, a franchisor must provide an extensive disclosure document which (among other things) sets out:

- important information about the franchise system and the franchisor
- arrangements which apply to resolve disputes
- arrangements which apply for the termination, renewal or non-renewal of a franchise agreement.

Issues to consider

- Research the concept, its marketability and the know-how required to make it a success.
- Some franchisors require franchisees to sign a contract containing many terms, which often favour the franchisor. Because the franchise idea is so valuable, the franchisor may dictate certain controls on the operation of the business which may be quite restrictive.
- Be aware of any contractual terms which might be anti-competitive.
- Will the owner franchisor provide the expected on-going support and other inputs which may help the business survive, for example, advertising and other promotional activity?
- Can you sell the franchise or does the franchisor have the first right of refusal?
- At the end of the franchise agreement will you be entitled to an exit payment? Will the franchisor buy any unused stock or assets from you at the end of the agreement? If so, at what cost?
- What kinds of changes can you make in the franchise business?
- What happens if the business or franchisor declines or fails?

Independent contractors

Definition

There is no clear cut definition of an independent contractor in Australia. The courts apply the common law which involves looking at the entire working relationship.

Generally, an independent contractor works to achieve specific results and maintains a high level of discretion and flexibility as to how work is performed. However, the contract may set out precise terms around materials used and methods of performance, and still be a contract for services.

Contracts with independent contractors

Before you sign a contract with a worker who you consider to be an independent contractor, you should clarify their status under the common law.

How does a worker's status affect the contract?

Different laws and mutual obligations apply to each type of relationship. For example, if your business is audited for Superannuation Guarantee and the worker you thought was an independent contractor, was actually an employee at common law, you could be fined and billed for Superannuation Guarantee owed to the worker. It is also illegal to disguise what is really an employment relationship as an independent contracting arrangement. This is called sham contracting. Even if the contract says a person is a contractor, they may be an employee under the Fair Work Act. Getting a worker's status wrong can also have implications for tax, workers' compensation and other laws that affect a contract.

Where to get further information

Visit www.business.gov.au/contractors.

- Visit the *Contractor decision tool*
- Download the publication, *Independent contractors: contracts made simple*
- Read the *Unfair contracts and sham contracts* page

Important things to consider

Get it in writing: It is advisable to put the contract in writing. This will minimise your risks and help to prevent disputes by clearly setting out the agreement before the work starts.

Intellectual property: It is important to note that unless the contract states otherwise, the intellectual property created by the contractor belongs to the contractor.

Description of services: The contract should state, in as much detail as possible, what work will be done, when the work will be done and where the work will be done.

Payments: The contract should set out whether payment will be by fixed fee or hourly/daily rate. Unless the contract is for a short duration, consider payments for completion of each stage—progress payments.

Dispute resolution clause: A contract should outline a process to assist in resolving disputes quickly without going to court.

Agency agreements

Definition

Basically, an agent is someone acting on behalf of a business, rather than acting on their own behalf.

Businesses rely on a range of people to act on their behalf, and these include employees, directors, partners as well as a range of professional agents who broker deals, find buyers and make purchases on behalf of the business. Estate agents, insurance agents and stock and station agents are examples of professional agents, but so are company secretaries and stock brokers, even though they do not use the word agent to describe their activities.

The legal relationship

The legal relationship of agency is when a principal (the business needing something done) authorises an agent to do certain things on behalf of the principal and which may include making contracts with an outside party.

Generally, the principal is legally responsible for the actions of their agent. It is therefore very important to define the scope of the agency in the agreement.

When an agent completes their task, they may leave the principal in a contractual relationship with the outside world.

Agents have a contractual relationship with the principal, which generally means they must do what the principal instructs and the principal in turn is obliged to pay for the services of the agent.

Agents also have a fiduciary duty to their principal, which is a relationship of trust requiring honesty, diligence and an undertaking to act in the best interests of the principal.

Types of agency agreements

Implied: Agency relationships may be implied by law, for example, partners under the Partnership Act of each State are specifically agents of the partnership and each other partner.

Informal: An agency agreement can be quite informal and ad hoc, for example, a fruit retailer, who is running short of supplies, may ring up a buying agent and ask them to look for particular products from a wholesaler (who is probably an agent for the grower).

Formal: Agency agreements can also be quite formal and may appear in a written form containing extensive terms. One formal type of agency is the appointment of a person with the **power of attorney.** These agents normally have a lot of discretionary power, perhaps even to run a business. Where large amounts of money are involved it is a good idea to formalise an agency relationship.

Differences between State governments

- The appointment of such agents is regulated differently in each State, with some States having specific legislation, for example, the Powers of Attorney and Agency Act in South Australia.
- Under various criminal provisions for the States there are penalties for agents taking secret commissions while working for their principal - in Victoria and New South Wales this is covered in their respective Crimes Acts.

9 Understanding the paper work

Where a contract involves substantial amounts of money, or will establish a long-term relationship, the negotiation period can be quite lengthy with various exchanges of correspondence until a final agreement is established. This section explains some of the most common exchanges.

The contract

Letter of Intention: A letter or note which indicates that the writer is intending to enter into an agreement or that they agree with whatever has been offered. Such letters may be sent to a successful tenderer or to someone making an offer. Letters of intention are generally considered under contract law as not sufficient to form a legal contract; they are preliminary to any proper agreement and care should be taken before commencing work or supplies under such a letter.

Comfort Letters: These are formal statements of assurance about the behaviour, integrity or the actions of a person, which are generally not intended to be legally binding. Take care if preparing these types of letters that it is clear whether or not the letter is supposed to be legally binding.

Memorandum of Understanding (MOU): Used as a preliminary step towards forming a binding agreement at a later stage. The purpose of an MOU is usually designed to demonstrate your interest in exploring a potential contractual relationship. As such, the MOU usually makes it clear that it is not intended as a binding agreement.

Heads of Agreement: Normally used to spell out agreement on the major issues of a contractual relationship prior to a comprehensive contract being put in place. They are not usually intended to be immediately binding unless the parties indicate otherwise.

Side letters: An agreement may be varied with the use of side agreements, or side letters, which sit outside a written public agreement. Side letters are useful to vary an agreement, if necessary, but cannot be used secretly to mislead or conceal the true nature of an agreement or arrangement.

Non-disclosure agreements: A business may require a potential contractor, or even employees, to promise not to disclose information which has been gained in a confidential relationship. What is actually confidential information is determined in law as that information which is not obvious, trivial or which someone may have had through their own professional knowledge, such as:

- strategic plans
- tenders
- prototypes
- pricing arrangements
- marketing plans.

10 Contracts which hold information

Privacy and Contracts

Information may be gathered and stored in the course of holding contracts of employment, in trade or for banking purposes. There are some general and specific laws which protect the privacy of individuals. A business which collects, uses or releases private details without consent may face legal action.

Particular areas to be wary of:

- Tax File Numbers - by law these must be kept secure and confidential
- Credit information - by law these must be kept secure and confidential
- Personal details of customers - should be stored appropriately and inappropriate information should not be collected or released to any unauthorised person or body
- Employee records - these must be kept confidential except to an appropriate authority.

Confidential Information

A business may hold valuable information which belongs to the business itself, or to another party. Information includes a range of commercial types such as data, plans, customer lists and trade secrets. A business may specify in contracts of employment or supply that no information is allowed to be disclosed, but this may also be implied by the nature of the relationship.

Confidential information is very specific and must be secret and known to be confidential. A business can use a number of legal actions against a person or organisation who misuses confidential information - since it is a breach of contract.

All businesses with a turnover of more than $3 million must comply with privacy principles and construct their own privacy rules, though some exemptions will apply regarding the release of information, for example, employee records. Some small businesses with turnover of $3 million or less also need to comply with the privacy principles. See the Office of the Australian Information Commissioner web site for details: http://www.oaic.gov.au

11 Intellectual Property and contracts

What is intellectual property?

Intellectual property is things such as any expression of ideas, designs, images, original writing and unique signs which have been especially created. The owner has exclusive rights and may be able to charge fees if anyone uses the intellectual property they have created.

Contracts containing intellectual property

A contract should not involve the use of someone's intellectual property unless there is permission to do so. Contravention of property rights could be direct or even indirect, e.g. linking to a website which carries images or words, or even sending writing, pictures or materials in a quote.

If a contract does not state who owns the intellectual property created during the life of the contract, the creator, who may be an independent contractor, will automatically own the rights.

Being Careful

If material is being used, referred to or copied, as part of a contract, then some checking should take place. Consider the following:

- Is the material of an exempt category, e.g. for education?
- Has permission been obtained?
- Has there been appropriate acknowledgment of the owner of the copyright?

Categories of Intellectual Property

Copyright:

Protected under the Copyright Act

Includes: published (original) works such as writing, music, recordings, films, computer programs, photos and music.

No registration is necessary and the owner has exclusive rights to use this material and collect fees for its use. Note:

- Copyright lasts 70 years after the death of the author
- Websites may contain copyrighted material, so be careful when copying this material.

Remedies for breach of copyright: stop orders, payments ordered by a court, fines, payment of profits and orders for destruction of works which infringe copyright.

Designs:

Protected under the Designs Act

Includes: original shapes, configurations, and patterns which might also be copyright

Designs can be registered with the Register of Designs. Note:

- Registration of design lasts for up to 10 years, if renewed after 5 years.

Remedies for breach of design: stop orders, payments ordered by a court, fines, payment of profits and orders for destruction of works which infringe an owner's design.

Patents:

Protected under the Patents Act

Includes: inventions which are new, novel and useful or something which significantly improves what existed before.

Patents can be registered with IP Australia but must be accompanied with specifications drawn by a patent attorney. Note:

- Registration can last up to 20 years
- Patents can be challenged as not original and therefore available to other eligible persons
- Patents can be registered internationally.

Remedies for breach of patent: a court can place a stop order on the use of a patent, an improper use of patent may result in an order to hand over profits.

Trade marks:

Protected under the Trade Marks Act

Includes: signs which indicate the ownership of a good or service. Signs include letters, words, names, signatures, numerals, devices, brands, labels, shapes, sounds or scents. Note:

- Registration can take place with IP Australia
- The trade mark must be distinguishable from others and not similar to any existing mark
- Registration lasts for 10 years.

Remedies for breach of trademark: court stop orders, orders for payments of damages and action for deceptive and misleading conduct.

12 Contracts completed using the internet

Electronic Transactions

Contracts can be made electronically by email or through an internet site, this is called e-commerce or electronic transactions. There are now two systems for making and proving a contract - the old paper system and the new electronic system. The making of contracts over the internet has exempted these contracts from some of the old law. There is now an Electronic Transactions Act in every Australian jurisdiction.

There are still many unresolved problems and the users of electronic means should be very careful in ensuring that the contract is clear and completed. It is not always clear who is making an offer or who is accepting. A business should have some procedure or system for checking on what is sent and received when making a contract, and who has authorised it at the other end.

The main principles

If a contract is made electronically then some special principles may apply. The essentials are:

- Definition of an electronic transaction: where data is sent by electro magnetic energy, including sound
- Where a contract has to be in writing at law: this may still be able to be satisfied by an electronic contract in some circumstances
- Giving information required by law: this may be able to be done electronically, e.g. issuing certificates, objections and lodging claims
- Signing a document: the parties to a contract can have an electronic signature or special means of identifying themselves
- Many contracts made electronically will be standard-form contracts. The law prohibiting unfair contract terms will apply if the other party is an individual and the contract is a standard-form “consumer contract”
- Production of a document: this may be done electronically if it can be shown to be the original document
- Recording of information: if required by law, this may be done in an electronic form in some circumstances
- Receiving a communication: this may be deemed to take place when the communication enters into the information system of the receiver - though the receiver may specify it must come to their attention to be a valid communication.

Note that the parties to the contract **must** consent to the use of these methods for it be valid. Think before you press the **I Agree** Button - what are you agreeing to?

13 Electronic Funds Transfer

The basic principles:

What is EFT?

Electronic Funds Transfer (EFT) is the paperless movement of money through the use of cards and the internet. Many businesses have arrangements (contracts) with financial institutions to pay for goods and services through a transfer system.

The cardholder:

A customer who uses a card has a contract with the financial institution regarding that card. The financial institutions have agreed that:

- Terms and conditions in using cards must be clear
- The cardholder will be notified of all charges in using the card and EFT facilities
- Cardholders may only be liable for a fixed amount if their card is lost or stolen (once they have notified the institution of its loss)
- Disputes go to the Financial Ombudsman Service

The Law:

The Payment Systems (Regulation) Act 1998 is particularly relevant to EFT. General law, contract law and the Australian Consumer Law also apply. Codes also exist to guide transfer processes - these include Banking Codes, Building Society Codes, and the Electronic Funds Transfer Code of Practice. Privacy law is also relevant. 'Merchants' have a contract with financial institutions which is quite separate from any contracts with a customer.

The Business accepting a card transaction:

Merchants who use the EFT system are normally required to sign a standard form contract which contains a number of provisions which include:

- The giving of a paper receipt
- To use reasonable care to detect forged signatures
- To allow a financial institution to debit the merchant's account with relevant charges
- To permit the financial institution to inspect books of account and records according to card transactions.

Merchants may charge a surcharge on any EFT transaction. If they do they must inform the customer of the surcharge before entering into the transaction and must not make misleading statements as to the reasons for it.

Schemes are not allowed to require that all their cards be honoured. For example a merchant may accept Visa credit cards but decline Visa debit cards.

The advantages:

If a business complies with the financial institution's terms. The financial institution then undertakes to pay into the merchants account the face value of all sales vouchers. The merchant gets to pass on risk to the financial provider, though there may be some exceptions, e.g. transactions through mail and telephone - which may move the risk to the merchant.

14 Resolving disputes with contracts

Thinking about a resolution

Clients of a business may occasionally have a dispute with that business. A business may also be in dispute with another business - businesses are consumers too!

Disputes over a contract should be addressed immediately or they can get out of hand and become worrisome, time consuming and expensive. Ultimately a dispute can go to court, but there may be some alternatives.

Some tips:

- Always listen to a complaint
- Attempt a resolution, compromise or some solution
- Don’t ignore correspondence on a complaint
- Weigh up the costs of reputation and legal advice against a compromise
- Seek advice on the legal situation.

Special Intermediaries

There are a variety of avenues in resolving disputes over contracts. Some special intermediaries exist who may be able to solve disputes without legal action, these include:

- The State Ombudsman
- The Commonwealth Ombudsman
- Financial Ombudsman Service
- An electricity or energy industry Ombudsman (depending on the State)
- A Legal Ombudsman (depending on the State)
- The Insurance Services Ombudsman
- The Telecommunications Industry Ombudsman
- Consumer Affairs bodies.

Alternatives to the courts

There are numerous tribunals and commissions at the State and Commonwealth level that may provide an alternative to formal legal action such as:

- The Small Claims Tribunal - which exists in different forms in different States, and
- The Office of Fair Trading (which can make recommendations and findings).

The dispute resolution process may involve mediation, conciliation, or arbitration (where the parties accept an independent decision).

Some bodies offer private resolution and mediation services and might negotiate an amicable resolution.

15 Bringing a contract to an end

Most contracts are concluded satisfactorily, goods and services are provided to the quality required and payments made as agreed.

When a contract comes to an end the parties involved have no further commitments to each other, with the exception of matters such as confidentiality and warranty provisions.

Bringing a contract to a premature conclusion, especially when it is also intended to seek compensation for non-performance, is something that should be contemplated only after other avenues have been considered and expert advice obtained. If you bring a contract to an end when you had no legal right to do so, you can be exposed to significant damages (for example, you may be required to compensate the other party for all its loss of profits).

The commercial reality is that this form of solution may not only remove any potential for further business with the other party - which may or may not be in your longer-term interest - but may well prove to be costly and very damaging. In the extreme situation of suing for non-performance, your business may suffer adverse publicity and attract, perhaps quite unfairly, a reputation as a difficult business partner.

Contracts can come to an end, or be brought to an end, in a number of ways – either by actions of the parties themselves, by some unexpected event or because the contract is found to be an unfair and unequal agreement.

Definitions - how a contract can end

Terms and their Definitions - how a contract can end

Agreement to end

The parties have agreed to end the contract - which means that they contractually agreed to end the contract and are bound by that decision.

Anti-competitive agreements

Certain “contracts, arrangements or understandings” between competitors, and some other anti-competitive activities, which limit the ability of businesses to compete or harm competition are prohibited.

Breach of contract

The refusal or inability to complete a fundamental term (condition) of the contract is a breach of contract and at common law may allow for the non-breaching party to terminate the contract - and potentially a claim for damages if there have been any losses or expenses as a result of the breach.

Children’s agreementsA person under the age of 18 is considered a minor and at law any contract with a minor may not be enforceable. Businesses are normally reluctant to hand over goods to a child, or to provide credit, without a guarantor.

Frustration

The contract has become impossible to carry out - the intention to complete an agreement has been frustrated by events beyond all parties’ control. A contract cannot be ended for frustration just because it has become inconvenient, difficult or expensive, or is going to cost more to complete.

Victoria, South Australia and New South Wales have legislation called Frustrated Contracts Acts, which basically provide a formula for sorting out payments and obligations after a ‘frustrating’ occurrence.

Case Study

Harry has been looking for a new car and after several months, signs a contract with Carsforsale to buy a silver sedan, with VIC registration ABC123. The contract says that the "risk in the car passes to Harry on signing the contract", even though the car has not yet been delivered to Harry. Unfortunately, two days after signing the contract, there is a fire at the car yard and Harry's silver sedan is destroyed before it can be delivered to him.

Generally, a contract may be frustrated on the basis of three categories of events being: the impossibility of performance of the contract, the frustration of the commercial venture or frustration of the purpose of the contract.

In this example, 'impossibility of performance' is relevant. A contract for specific goods (such as Harry's new car) will generally be frustrated for impossibility of performance if the goods are destroyed before risk passes to the buyer. However, in Harry's case, as the contract stated that risk passed to Harry as soon as he signed the contract, the car was actually destroyed after risk had passed to him despite the fact that it had not been delivered to him. In this situation, the contract will not be frustrated.

Terms and their definitions

Illegality

The carrying out of the contract is illegal - so by law it cannot be continued.

Mistake

In rare cases, if the agreement is based on a fundamental mistake or mistaken belief about property agreed upon, the contract may be ended. Sometimes an agreement is reached and then the parties discover that the property no longer exists, or they were contracting for entirely different things.

Performance

The contract has been completed by all parties according to the agreement.

Pressured agreements

If a person has only entered an agreement because of threats, harassment, fear or actual force (duress), this may result in the ending of the contract. This is distinct from legitimate commercial pressure such as raising prices during a shortage.

Unconscionable agreements

Unconscionable behaviour in making an agreement may include unjust, unfair or unscrupulous conduct which is considered contrary to community standards. In practice, however, it is narrowly defined.

In business-to-business contracts, a business (not a publicly listed company) may allege unconscionable conduct where a stronger party has exploited its bargaining power to impose contractual terms or engage in conduct that would be unreasonable in the context of a particular commercial relationship.

Unconscionable contracts can be brought to an end under the Australian Consumer Law if there has been unacceptable behaviour by a company.

16 Renegotiating a new contract on same / similar terms

Case Study

Sam owns a small business in Canberra and contracts with Bill's Stationery Company. The contract ended last week. Sam was very happy with the contract as the prices were very cheap and he is hoping to renegotiate a new contract with Bill's Stationery on similar terms. Bill tells Sam that he needs some time to consider the terms of the contract, including his prices because his costs have gone up, however, he is happy to agree to negotiate with Sam.

They decide to sign a document called a 'heads of agreement' which contains a number of terms and conditions for the future supply of office stationery. The heads of agreement says that they will negotiate in good faith to agree a more comprehensive and detailed supply agreement, which, when executed, will replace the heads of agreement. The heads of agreement does not stipulate the price that Sam will pay for the supplies as he and Bill have not yet agreed on this point.

Agreements to negotiate, or agreements to enter into a contract are generally not binding contracts. In some circumstances however, the courts have considered that in principle, parties who have expressly bound themselves to negotiate in good faith should be held to that promise where the heads of agreement or other preliminary agreement is not uncertain, vague or incomplete. Potentially, this means that if Sam and Bill have set out the important terms of the contract, for example, the price to be paid for the supplies, the heads of agreement could be upheld as a binding contract.

17 Summary checklist

Regardless of the specific nature of the contractual issue, there are a few key questions which you need to ask yourself that can help identify and clarify:

- whether the contract meets your objectives
- which matters are of primary importance and which are of secondary or lesser importance
- the potential risks in the relationship
- what the contract must clearly protect.

Time spent thinking about them beforehand can save a great deal of grievance and expense later while at the same time maximising the quality of any time spent with your legal advisor.

☐ **What do you want out of the relationship?**

- How important is it to you?
- What commercial return do you require over what period of time?
- Does it have the potential to grow?
- Does it have strategic value? Can it be the stepping stone to bigger things?
- How long do you want it to last?

☐ **What does the other party want?**

- How important is it to them?
- Do they see it having the potential to grow?
- Does it have strategic value to them? Can it be the stepping stone to bigger things?
- How long do they want it to last?

☐ **What issues are absolutely critical to you about which you could not compromise (in the contract conditions)?**

- Reliability of supply
- Price
- Cost of credit
- Volume of business
- Market share
- Market exposure
- Other

☐ **Have your expectations and 'bottom line requirements' been made clear to the other party during the process of negotiation?**

- Do they clearly understand your position?
- Are they prepared to accommodate your critical requirements?
- Are they capable of accommodating your critical requirements?

☐ **Understanding each party's needs and expectations, how far are you willing to compromise on such issues as:**

- The availability of credit terms
- Frequency of price review
- The means of calculating price reviews

☐ **What level of risk is involved and who bears it?**

- What is the commercial reputation of the other party?
- What could go wrong in the relationship that could seriously affect your business?
  - Failure of the other party's business
  - Inadequate marketing support
  - Change of ownership in the other party's business
  - Magnitude and frequency of interest rate/rental/invoice price adjustments
  - Resignation/death of key personnel
  - Delays in delivery
  - Delays in payment
  - Inferior or inappropriate quality
- Have these issues been addressed in the contract?

☐ **How possible is it for things to go wrong?**

- What is industry experience?
- How many 'steps' in the chain?
- Where are you most vulnerable?

☐ **Remember some basic rules - look at the fine print**

- Written contracts, where practical, are always the best form of contract to rely on.
- Keep records of any promises made to clients by parties acting for the business - this could be done on a standard form showing dates and times.
- You may find it useful to construct a model contract which can be filled in by the party at the time an agreement is made - this would ensure that you always have something in writing.

Make sure that:

- anything signed by the parties making the agreement is the same as the spoken agreement made
- any changes made to an agreement are explained and documented with the other parties
- all parties have a copy of the contract, along with the appropriate changes
- any difficulties or defects regarding a product or service have been brought to the attention of all parties.

Take special care:

- when dealing with people who might be disadvantaged in terms of sight, hearing or language capabilities - so that they understand the contract, or at least have had legal advice
- to be aware that contracts are regulated by unconscionable conduct provisions under the Australian Consumer Law
- in expressing an opinion - particularly where it may be relied on as the basis of the agreement
- when dealing with competitors, not to agree to fix prices, share markets, rig bids or restrict outputs
- not to directly or indirectly fix the minimum price at which a person may resell goods, or to supply goods or services on condition that other goods/services be acquired from a third party.
    - Read everything **before** you sign it.
    - Seek professional advice where you are unsure of the meaning or consequence of any contractual issue, especially if:
- a substantial amount of money is involved
- your possible liability under the contract is substantial
- further similar situations are likely to arise
- the other party is using professional advice.

18 Additional sources of information for small businesses

www.business.gov.au

The business.gov.au website is an online government resource for the Australian business community. By using business.gov.au, businesses will know how to comply with government requirements more simply and conveniently.

The website provides range of services including ABN Lookup, taxation compliance and license applications.

Through business.gov.au you can:

- access a wide range of services and information about start-up, taxation, licensing and legislation
- search from a wide range of government grants, assistance and advisory services
- find, manage and complete the forms online with all levels of government
- use the ABN Lookup service to search for the Australian Business Number details of creditors and debtors
- tailor your search for information to suit your business and area of operation, and
- privately and securely undertake a number of initial business registrations with the Australian Taxation Office and the Australian Securities and Investment Commission on-line.

To see how business.gov.au can help your business, visit our website www.business.gov.au today.

Small business advisory offices (State and Territory)

Government-funded small business advisory services operate in most States and Territories. Each offers free information, advice and referral services. These services should be consulted during the planning and establishment phases of any small business venture. Specific services vary between organisations but the following services are generally provided:

- information and referrals;
- free, impartial and confidential services provided by experienced personnel; and
- a large selection of inexpensive, easy to read publications covering all aspects of small business operation and management.

The Australian Government also funds a Small Business Support Line, which provides initial advice to small business owners and puts them in touch with specialist advisers on matters such as obtaining finance, cash flow management, retail leasing, diagnostic services, promotion and marketing advice, and personal stress/hardship counselling. Support Line advisors link into the nationwide network of Business Enterprise Centres and other small business advisory services around Australia.

The Support Line can be accessed on 1800 777 275 between 8am and 8pm AEDT weekdays, by email at sbsl@innovation.gov.au or via Live Chat on the www.business.gov.au website.

Small businesses can also access essential government information and resources on the Small Business Resource Kit which can be ordered through the Small Business Support Line on 1800 77 7275 or by email sbsl@innovation.gov.au

NEW SOUTH WALES

Small Business NSW
NSW Trade and Investment
Level 47 MLC Centre
19 Martin Place
Sydney NSW 2001
Tel: (02) 9338 6600 / 1300 134 359
http://www.smallbiz.nsw.gov.au

VICTORIA

Business Victoria
121 Exhibition Street
Melbourne Vic 3000
Tel: 13 22 15 / (03) 9651 9999
http://www.business.vic.gov.au

SOUTH AUSTRALIA

Department of Trade and Economic Development
The Conservatory
131-139 Grenfell Street
Adelaide, SA 5000
Tel: (08) 8203 2400
http://www.southaustralia.biz

TASMANIA

Department of Economic Development
Level 1 Reception
22 Elizabeth Street
Hobart TAS 7000
Tel: (03) 6233 5888 / 1800 440 026
http://www.development.tas.gov.au

AUSTRALIAN CAPITAL TERRITORY

Business Development
Level 2 Telstra House
490 Northbourne Avenue
Dickson ACT 2602
Tel: 1800 244 650
http://www.business.act.gov.au

QUEENSLAND

Department of Tourism, Major Events, Small Business and the Commonwealth Games
Level 26
111 George Street
Brisbane Queensland 4000
Tel: 13 25 23 / (07) 3225 2003
http://www.business.qld.gov.au/

WESTERN AUSTRALIA

Small Business Development Corporation
Level 2
one40 William Building
140 William Street
Perth WA 6000
Tel: 13 12 49 / (08) 6552 3300
http://www.sbdc.com.au

NORTHERN TERRITORY

Department of Business and Employment ,
Ground Floor
Development House
76 The Esplanade
Darwin NT 0800
Tel: 1800 193 111 / (08) 8999 6888
http://www.nt.gov.au/dbe/