

Explain what is meant by an unfair term in a contract and describe and evaluate the effect(s) thereon of the Unfair Terms in Consumer Contracts Regulations 1999.

After the Treaty of Maastricht, the European Community made a directive on Unfair Terms in Consumer Contracts 1993. This instructed member states to pass domestic legislation to provide consumer protection. As a result, the UK Government made the Unfair Terms in Consumer Contracts Regulations 1994 which have now been replaced by the Unfair Terms in Consumer Contracts Regulations 1999. The main aim of the new regulations is for UK Law to be drafted more closely to the wording of the European Legislation, to help prevent discrepancies between the two. The principle change from the 1994 regulations and the 1999 regulations are simply that more institutions are now able to enforce the legislation, beyond the Director-General of Fair Trading.

An unfair term is defined in Regulation 5(1) of the Unfair Terms in Consumer Contracts Regulations 1999 as;

‘ A contractual term which has not been individually negotiated shall be regarded as unfair if, contrary to the requirement of good faith, it causes a significant imbalance in the parties rights and obligations arising under the contract, to the detriment of the consumer’¹

In addition to this Reg 6 of the same Regulations states that,

‘the fairness of a contractual term shall be assessed, taking into account the nature of the goods or services for which the contract was concluded and by referring, at the time of conclusion of the contract and to all the other terms of the contract or of another contract on which it is dependent.’²

Schedule 2 of the 1999 regulations contains a list of 17 non exhaustive and indicative terms which are reputably considered to be unfair; this list is identical to that of the list contained in the 1994 Regulations except for one aspect. The earlier list, referred to clauses which enabled a business to alter unilaterally the contract terms without a valid reason being specified in the contract. This was then qualified to exclude

¹ Unfair Terms in Consumer Contracts Regulations 1999 Reg 5(1)

² Unfair Terms in Consumer Contracts Regulations 1999 Reg 6

changes in interest rates in contracts with a supplier of financial services. This exception has now been removed, so that consumers have a better chance of challenging the fairness of a clause in a contract for the provision of financial services.³

The 1999 Regulations does not have a list of factors which are to be taken into account when assessing the issue of good faith or unfairness which is present in the 1994 Regulations. The 1999 Regulations simply say that the fairness of a term is decided in the light of the circumstances at the time of making the contract.

As stated in Reg 5 for a term to be deemed unfair, the significant imbalance it generates must be contrary to good faith. Good faith is likely to require that contracting parties deal with each other in an open and honest way, taking into account their relative bargaining skills.⁴

In the case of *Interfoto Picture Library Ltd V Stiletto Visual Programmes Ltd* 1989, [1988] 1 All ER 348, Bingham LJ⁵ summarised the position. Most legal systems outside the common law enforce an overriding principle that parties should act in good faith when making and carrying out contracts. This does not simply mean that they should not deceive each other, but is in essence a principle of fair and open dealing. English law had committed itself to no such overriding principle, but had developed piecemeal solutions in response to demonstrated problems of unfairness.

One other strange feature of the definition of an unfair term is that no assessment must be made of the fairness of any term which defines the main subject matter of the contract or which concerns the adequacy of the price or remuneration, as against the goods and services supplied in exchange, in so far as these terms are in plain intelligible language⁶ It may seem peculiar that these terms are excluded from the fairness requirement, but it has been suggested that the aim of the Regulations is to attack what may be called 'unfair surprise'⁷ that is to say consumers tend to be aware

³ C Elliott and F Quinn, *Contract Law* 3rd Ed 2001 pg 123

⁴ C Elliott and F Quinn, *Contract Law* 3rd Ed 2001 pg 123

⁵ Bingham LJ, *Interfoto Picture Library Ltd V Stiletto Visual Programmes Ltd* 1989, [1988] 1 All ER 348.

⁶ Unfair Terms in Consumer Contracts Regulations 1999 Reg 6(2)

⁷ E Mc Kendrick, *Contract Law* 4th Ed 2000 pg 367

⁸ *Director- General of Fair Trading v First National Bank PLC* (2002) 1 ALL ER 97

of the price of the goods or services and the definition of the main subject matter of the contract but they tend to be unfamiliar with the countless terms found in the small print, which are the subject of regulation. In the case of *Director- General of Fair Trading v First National Bank PLC* (2002)⁸, Lord Goodhart QC, on behalf of the bank, submitted that no assessment might be made of the fairness of the term because it concerns the adequacy of the bank's remuneration as against the services supplied, namely the loan of money. A bank's remuneration under a credit agreement is the receipt of interest. The term, by entitling the bank to post-judgment interest, concerns the quantum and thus the adequacy of that remuneration. This was the more obviously true if, as Lord Goodhart submitted, the merger rule as commonly understood is unsound. Where judgment is given for outstanding principal payable under a loan agreement and interest accrued up to the date of judgment, those claims (he accepted) are merged in the judgment. That is a conventional application of the principle of *res judicata*. But no claim for future interest has been the subject of adjudication by the court and such a claim cannot be barred as *res judicata*. The borrower's covenant to pay interest on any part of the principal loan outstanding thus survives such a judgment, and *Ex p Fewings* (1883) 25 Ch D 338 was wrong to lay down any contrary principle. Lord Goodhart adopted the observation of Templeman LJ in *Ealing LBC v El Isaac*⁹

Where a term is held to be unfair, the consequences is that it 'shall not be binding on the consumer' but the 'contract shall continue to bind the parties of it is capable of continuing in existence without the unfair term' Regulation 7 further states that a seller or supplier shall ensure that any written term of a contract is expressed in plain intelligible language and if there is any doubt about the meaning of a written term, the interpretation most favourable to the consumer shall succeed.

The effect of a term being found to be unfair in accordance to the 1999 Regulations in set out in Reg 8(1) that, 'unfair terms in a contract are not binding on the consumer'¹⁰,

⁹ [1980] 2 All ER 548 at 551, [1980] 1 WLR 932 at 937.

¹⁰ Unfair Terms in Consumer Contracts Regulations 1999 Reg 8(1)

¹¹ Unfair Terms in Consumer Contracts Regulations 1999 Reg 8(2)

¹² P Richards, *Law of Contract*, 5th Ed 2001

thus it is the individual term that is avoidable not the contract as a whole. This is subject to the proviso in Reg 8(2) that the rest of the contract is capable of continuing in existence without the unfair terms.¹¹

The regulations try to preserve the notion of freedom to contract by first of all if the contract is individually negotiated then the contract will fall outside the regulations, second of all if a consumer has exerted any influence on a contract term within a standard form contract it will be assumed that the term will not be unfair, although the regulations will apply to the rest of the contract, lastly the regulations exclude terms that define the main subject matter of the contract and relate to the adequacy of the contract price from the ambit of the regulations, though such terms still have to comply with the general requirement of reg 7 that they are drafted in plain intelligible language.

Article 7(1) of the directive provided that Member States have to ensure that adequate and effective means exist to prevent the continued use of unfair terms in contracts concluded with consumers. Also Article 7(2) states that there must be a means by which any person or body that has a legitimate interest in protecting consumers can challenge that 'contractual terms drawn up for general use are unfair'¹²

The major change made by the re-issue of the Regulations is in enforcement. The new Regulations maintain the Director General's power to take injunctive action against terms he considers unfair¹³. But this power is also extended to a number of other 'qualifying bodies'. These bodies are named in Schedule 1 to the Regulations, which is split into two parts. Part 1 lists public authorities that have a statutory basis, including most of the main national regulatory bodies, and all local authority trading standards departments. Part 2 is reserved for independent bodies, and currently includes only the Consumers' Association.

¹³ Unfair Contract Terms; A case report bulletin issued by the Office of Fair Trading Issue No 8 December 1999

It remains the case that only the Director General has an unqualified duty under the Regulations to consider and deal with complaints about unfair terms, and to give reasons for his decision to apply or not to apply for an injunction. The ‘qualifying bodies’ listed in part 1 of Schedule 1 may come under such a duty, but only if they choose to accept it. Until and unless they notify the Director General that they agree to deal with a complaint, they are bound only by the usual requirements of administrative reasonableness and fairness.

All qualifying bodies are subject to notification requirements about cases they decide to pursue, and the Director General is subject to new publication requirements. Together they make the Director General of Fair Trading the focal point for holding and publishing information about enforcement.

Further changes have been made to the enforcement regime under the Regulations. Firstly, Injunctive action under the Regulations may now be taken in the County Court, not merely as under the 1994 Regulations in the High Court. This is expected make it easier for local authorities to take enforcement action. The right to issue court proceedings was first used in the case of Director- General of Fair Trading v First National Bank (2000), the case was about a clause in the banks standard loan agreement which stated: Interest on the amount which becomes payable shall be charged in accordance with condition 4, at the rate stated in paragraph D overleaf (subject to variation) until payment after as well as before any judgment (such obligation to be independent of and not to merge with the judgment).¹⁴ At first instance the trial judge decided that this term was not unfair, but the Court of Appeal disagreed in the light of the inequality of bargaining power between the contracting parties and took a broad approach to the issue of fairness.¹⁵

The second further change was, the Director General and the statutory qualifying bodies were given power by Regulation 13 to require disclosure of documents and information where this is necessary for enforcement purposes. It is expected that this

¹⁴ Director- General of Fair Trading v First National Bank (2000)

¹⁵ C Elliott and F Quinn, Contract Law 3rd Ed 2001 pg 124

will significantly improve the monitoring of compliance with undertakings given to drop or amend contract terms.

In conclusion I would say that the effect of the Unfair Terms in Consumer Contracts Regulations 1999 on whether a term is to be deemed fair or unfair prevents an injustice on consumers who may not have strong bargaining power against larger corporations. The regulations have also given more qualifying bodies the right to take action against unfair contracts which will most likely help decrease the level of unfair terms in future contracts and greater equality for consumers.

An advantage of the 1999 regulations is that they take into account the previous 1977 and 1994 regulations which mean that there is greater protection for consumers from unfair terms.

The fact that the regulations are confined in their scope to consumer contract means that it is kept out of the commercial sphere where the need for certainty is greatest. So the uncertainty which the regulations will initially create is not the grave cause for concern which it would be if it applied to international contracts for the sale of goods.¹⁶

Overall the 1999 Regulations have had a significant effect on unfair terms, which will must likely result in a decrease of unfair terms being used in contracts.

¹⁶ E Mc Kendrick, Contract Law 5th Ed 2003 pg 282

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