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Sent via email to: sean.browne@bis.gsi.gov.uk

Dear Sean

The City of London Law Society response to the Department of Business, Innovation and Skills document “Protection of Small Businesses when Purchasing Goods and Services: Call for Evidence”

The City of London Law Society (“CLLS”) represents approximately 15,000 City lawyers through individual and corporate membership including some of the largest international law firms in the world. These law firms advise a variety of clients from multinational companies and financial institutions to Government departments, often in relation to complex, multi jurisdictional legal issues.

The CLLS responds to a variety of consultations on issues of importance to its members through its 19 specialist committees. This document is a response to the Department of Business, Innovation and Skills’ document “Protection of Small Businesses when Purchasing Goods and Services: Call for Evidence” the consultation period for which commenced on 24 March 2015 and ends on 30 June 2015.

This response is given by the CLLS Commercial Law Committee. The committee is strongly against the proposals contained in the call for evidence, and we have given our responses by reference to answers to selected questions.

1. **Executive Summary**

Extending consumer protections to Micro and Small Businesses (“**MSB**”s) is likely to create legal uncertainty and increase the financial and administrative burden for businesses (including MSBs, who act as both customers and suppliers) by creating a two-tiered system with separate applicable terms and conditions, as well as an ongoing obligation to verify whether a business continues to qualify as an MSB.

2. **Costs and Benefits**

2.1 *Q.4 What examples are there of advantages with the current arrangements?*

The current arrangements create a relatively clear distinction between businesses and consumers. This is echoed in the definition of “consumer” in the Consumer Rights Act 2015 as “an individual acting for purposes that are wholly or mainly outside that individual’s trade, business craft or profession”. This distinction is based upon the purpose of the contract, rather than the nature of the party contracting. For example, an individual who is a sole trader and contracting in the course of his/her business will be treated as a business, rather than as a consumer, despite still being an individual.

With this clear distinction, business to business (“B2B”) suppliers (including MSBs) benefit by having a uniform statutory framework applying to their supply contracts and as a consequence can have one set of terms and conditions in place for all customers.

While in certain sectors (such as energy, telecommunications and consumer credit) small businesses have been extended some consumer-like protections, these are specific environments and the extensions have been targeted and limited in nature.

To scale the extension of consumer protections to MSBs to include all contracts with MSBs would create significant problems, as set out in more detail below.

2.2 *Q.5 Are these advantages one-off examples, or are there advantages which are ongoing, or which occur in certain sectors?*

These advantages are ongoing, across all sectors.

3. **Position of suppliers to MSBs**

3.1 *Q.29 Would different rights and remedies for MSBs affect the business models of suppliers, both other MSBs and larger firms?*

It is proposed to extend consumer rights and remedies with respect to the supply of goods and services to MSBs that act as customers. We assume that the proposed extension will not exempt MSBs who act as suppliers.

First and foremost, the proposed extension creates legal uncertainty for MSBs. As stated in the call for evidence, MSBs make up 99% of all businesses in the UK. The majority (if not all) of these MSBs are suppliers as well as customers. As such, any extension of consumer protection of this nature would be a double-edged sword. This may result in increased legal spend by MSBs to ensure compliance, or increased confusion about the application of the statutory regime.

The proposed extension may create difficulty with long-term supply agreements with MSBs, as it is anticipated that many MSBs would grow out of the definition of MSB throughout the course of an agreement. It would be unfair if larger businesses continued to benefit from the extended protections, simply because they started as MSBs.

We foresee similar problems with agreements that automatically renew. Would businesses need to certify their MSB status before each such renewal?

We note that this may serve as a deterrent to contracting with MSBs, by imposing an extra burden on suppliers. Suppliers (whether MSBs or larger firms) would either need to adjust their business practice to contractually provide these remedies to all business customers or (more likely) have at least two versions of its terms and conditions, to cover both MSBs and larger firms. Determining which terms and conditions would apply to which customers would increase expense and uncertainty for both parties.

Finally, the different rights and remedies for the supply of goods and services may have a chilling effect on e-commerce, by requiring online businesses to rely upon customer self-certification as to MSB status. What would be the effect of self-certification in error? How will these online businesses deal with MSBs that grow beyond 9 employees and no longer qualify for the additional protections?

3.2 *Q.30 Would it be costly for suppliers to distinguish between MSBs and other customers?*

As mentioned above, the different rights and remedies would need to be reflected in the terms and conditions of supply. As such, the suppliers would need to perform due diligence as to whether the customer is an MSB. At the very least this would involve the added administration and expense of verifying (pre-contract) the employment numbers of the potential MSB (for example, through annual HMRC return or self-certification by the potential MSB).

In addition to the above, we assume BIS would include provisions to exclude from the extension of the consumer rights SPVs, group companies of larger companies as these are either themselves highly sophisticated or can call on group resources) and higher value contracts (as proposed in the joint Law Commissions report in 2005). As such, the due diligence in question would not be confined to establishing the number of employees, but also verifying control of the potential MSB. Establishing whether these exclusions apply is less straightforward than simply verifying the number of employees, as it involves interrogation of the potential MSB's constitution and shareholding, as well as looking at potential transaction value. This higher level of due diligence would increase the supplier's costs significantly.

Finally, MSBs tend to grow quickly if successful, which creates an ongoing compliance obligation on the supplier, if there is an established relationship between the MSB and supplier (for example a framework agreement). Therefore, the due diligence is not simply a one-off expense, but rather an ongoing process.

4. Application of consumer rights

4.1 *Q.33 We are interested in views, with supporting evidence, on any of the protections—in responding, these need not be considered as a package. The key protections are set out in Part 3, but in summary these are:*

- *rights and remedies in relation to contracts for goods;*
- *rights and remedies in relation to contracts for services;*
- *rights and remedies in relation to contracts for digital content;*
- *terms limiting liability for key protections being automatically non-binding;*
- *right to challenging certain terms as unfair;*
- *requirements to provide certain information before a contract is made;*
- *right to withdraw from distance and off-premises contracts.*

As mentioned above, the extension of the rights and remedies in relation to goods, services and digital content, would create legal uncertainty for the parties and impose an additional burden on the suppliers (many of which would be MSBs).

The extension of unfair contract terms protection to MSBs, would have a similar effect, creating two different laws applicable to businesses in a B2B environment (even where the supplier is an MSB), and resulting in different applicable terms and conditions, depending on the size of the customer. The mechanisms in UCTA are already adequate (and appropriate) for creating balance between B2B parties where otherwise there is a risk of imbalance,

specifically the fact that certain limitations of liability are subject to a reasonableness test in which the bargaining position of the parties is a factor (as noted in the call for evidence). As a consequence of UCTA, suppliers are aware that even where a B2B contract has been negotiated, then a customer with little bargaining power will still have some protection against certain limitations of liability. Similarly, when drafting B2B standard terms and conditions of sale, suppliers are aware of the ways in which UCTA fetters their ability to limit or exclude liability in some situations.

Accordingly, on two levels (via the reasonableness test and through the enhanced controls in relation to B2B contracts on the supplier's standard terms) UCTA seeks to redress imbalances in bargaining power. In fact, focusing on bargaining power rather than simply the size of the purchasing company is a much better way of introducing fairness. A company is likely to have more bargaining power in some purchasing situations than others (as a result of the nature and size of the purchase, for example) regardless of the size of the company. The current arrangements reflect that.

The right to withdraw from distance and off-premises contracts, was designed to address concerns unique to consumers (for example, door-stepping), and are less applicable (if not inapplicable) to businesses.

Finally, based upon the reasoning behind the extension of consumer protections, we question why BIS is considering extending these protections to MSBs and not to other organisations (such as non-profits, social enterprises and charities) which may exceed the employee threshold but may be similarly or even more commercially unsophisticated?

- 4.2 *Q.34 Alternatively, is there evidence that regulating MSBs with consumer legislation might have unintended consequences, e.g., chilling effect on the willingness of firms to enter contracts or costs associated with their being less flexibility in contracts etc.?*

See our comments above in relation to e-commerce.

We also consider there to be a risk that larger firms may refuse to contract with MSBs to avoid the added risk and expense. This would obviously have a negative effect on MSBs by restricting access to goods and services, which may potentially be necessary for carrying on business.

In light of the above we strongly oppose the proposals contained in the call for evidence.

Should you have any questions about the above, please contact Oliver Bray (Chairman) or Richard Marke (Secretary) at oliver.bray@rpc.co.uk or r.marke@bwbllp.com

Yours sincerely

Oliver Bray, Chairman

Date: 30th June 2015

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**THE CITY OF LONDON LAW SOCIETY
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