THE LAW SOCIETY
OF NEW SOUTH WALES

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28 August 2014

Committee Secretary
Senate Economics References Committee
PO Box 6100
Parliament House
Canberra ACT 2600

By email: economics.sen@aph.gov.au

Dear Committee Secretary,

Inquiry into the need for a national approach to retail leasing arrangements

The Law Society's Property Law Committee ("Committee") is pleased to respond to the invitation to comment in relation to the Senate Economics References Committee Inquiry into retail leasing arrangements.

The Committee is comprised of specialist property law practitioners, including practitioners who act for landlords and tenants, large and small.

Retail tenancy legislation is State-based, combining aspects of real property law and tenancy law. The Committee notes that significant work has been undertaken by the Law Society and the Law Council of Australia to transition to a national property law in relation to two current projects: national electronic conveyancing, and the Uniform Torrens Title Act projects. Accordingly, the question of whether there is a need for a national approach to retail leasing arrangements is quite timely. In the Committee's view a national legislative approach to retail tenancy legislation must be considered in the context of a national approach to property law as a whole. Without this greater context, a move to national retail leasing legislation could introduce a further level of complexity which would be undesirable for all participants in the industry.

Clearly a move to a national legislative approach to retail tenancy legislation will benefit landlords and tenants who operate in more than one jurisdiction. Currently landlords and tenants who operate nationally need to be cognisant of the significant variations in legislation across the jurisdictions. Moving to a national framework for retail tenancy legislation should reduce compliance costs and increase the ease with which landlords and tenants could seek to broaden their operations across different States.

In this context, the Committee broadly supports the transition to a national approach to retail leasing arrangements. The Committee notes that previous reviews have recommended a transition to a national approach for retail leasing arrangements, most notably the final report of the Australian Productivity Commission dated 27 August 2008 *"The Market for Retail Tenancy Leases in Australia"* ("PC Report 2008").

For small operators, only operating within one jurisdiction the question of whether the relevant legislation is national or State-based is a moot point. For such smaller operators the question of compliance is much simpler but the question of whether the legislation is unduly prescriptive is of equal importance.

The PC 2008 Report amongst other recommendations favoured a reduction in the prescriptiveness of legislation to assist the move to a nationally consistent retail lease framework. Whether or not this has occurred in other jurisdictions is something that the Committee is unable to comment on.

In New South Wales several reviews of the *Retail Leases Act 1994* ("the Act") have taken place, including the current incomplete review which formally commenced with the issue of a Discussion Paper in 2013 by the Office of the Small Business Commissioner *2013 Review of the Retail Lease Act 1994* ("NSW Discussion Paper"). The Committee notes that a number of the issues raised in the NSW Discussion Paper have also been raised as terms of reference for the Senate Economics References Committee's current Inquiry.

Although the New South Wales legislation makes it very plain that the Act is to be reviewed after seven years, the history of review is more appropriately described as *ad hoc*, creating much business uncertainty. Any move to a national framework should only be attempted with a clear mandate from all participating jurisdictions otherwise it too may create undesirable business uncertainty.

The Committee does not support harmonisation for its own sake without due consideration to best practice and qualitative considerations. The Harmonised Disclosure Statement is a recent example of a harmonisation project which did not, in the Committee's view, provide any real benefit. This may have been due in part to the absence of consultation in New South Wales and the short timeframe between gazettal, re-gazettal (to correct a typographical error) and commencement. Harmonisation alone is not a sufficient reason to make substantial changes to current practice. Any development of a national legislative framework should be undertaken with due consideration of whether current prescriptive requirements actually fulfill their intended original purpose or whether such requirements add to the cost of compliance without any real gain for either party to the leasing transaction.

The Committee sets out some brief comments in relation to the specific terms of reference of the Senate Economics References Committee Inquiry as follows:

1. The first right of refusal for tenants to renew their lease

The Committee does not support legislation providing a first right of refusal for tenants to renew their lease. Proponents of a first right of refusal assert there has been a market failure where the tenant has been unable to negotiate a new lease at the end of a term. In the Committee's view this is not a matter of market failure but more likely market forces at work. If the market is favouring landlords, a particular landlord may not want to negotiate with an existing tenant and might seek to find a better tenant. Conversely, if the market is favouring tenants, a particular tenant may seek to negotiate a more advantageous lease elsewhere. There could be a myriad of reasons as to why a new lease is not offered or not sought.

A right of first refusal is often premised on the basis that it provides a tenant with a greater security of tenure. However, in the Committee's view, security of tenure is better assisted by requirements for both parties to the lease to give adequate notice

to each other of their future intentions such that appropriate negotiations can begin well prior to the end of the current lease.

2. Affordable, effective and timely dispute resolution processes

The importance of affordable, effective and timely retail lease dispute resolution processes cannot be underestimated. The personal and commercial costs in delaying dispute resolution are particularly marked in this area. In New South Wales dispute resolution processes appear to be working reasonably well and are strongly linked to the provision of appropriate information and education by the New South Wales Office of the Small Business Commissioner.

Jurisdiction for retail lease disputes is shared between the New South Wales Civil and Administrative Tribunal ("NCAT") and the New South Wales Supreme Court. Whether or not NCAT's current jurisdictional monetary limit of $400,000 should be increased is one of the issues raised in the NSW Discussion Paper. The Committee regards the current jurisdictional monetary limit as appropriate. However the Law Society's Dispute Resolution Committee is concerned that the jurisdictional limit of $400,000 for hearing retail leasing disputes in NCAT is too low given the typical quantum of claim and considers that the jurisdiction should be increased to $750,000, so that parties may avoid commencing proceedings in the Supreme Court.

3. A fair form of rent adjustment

Presumably this term of reference is referring to the manner in which rent is reviewed during the term of the lease. Commonly rent reviews are based on CPI increases or a fixed percentage; sometimes there is a market review during the term of a lease or upon the exercise of an option. The form of rent review should be determined by the parties in that particular market.

The Committee also notes that most jurisdictions prohibit ratchet clauses and it would envisage that this would remain the case in the foreseeable future.

4. Implications of statutory rent thresholds

The Committee notes it would be beneficial to harmonise jurisdictional thresholds in relation to rental costs. For example the Committee notes that the *Retail Leases Act 2003 (*Vic*)* does not apply to premises where the occupancy costs (rent, other than percentage rent, plus prescribed outgoings, as estimated by the landlord) exceed $1,000,000 per annum. The NSW legislation does not contain a rent threshold, but does exclude premises that have a lettable area of 1000 square metres from the requirements of the Act.

The Committee also suggests it would be beneficial to harmonise across the jurisdictions whether public company tenants have the benefit of protections provided by retail leasing legislation.

5. Bank guarantees

The Committee notes that bank guarantees are commonly used as a means of providing security for the tenant's obligations under the lease. The Committee does not consider it is appropriate for legislation to deal with the drawdown of a bank guarantee as this is a matter between the landlord and the issuing bank and subject to the terms of the lease itself. In New South Wales there have been recent discussions as to whether there should be a timeframe after the end of the lease within which the landlord must release the bank guarantee. However, in the Committee's view the bank guarantee should only be returned once the tenant has

complied with its obligations under the lease; to do otherwise undermines the giving of security in the first place.

6. A need for a national lease register

In the current review of the Act in New South Wales, the concept of a register for a summary sheet of retail leases has been proffered. The Committee does not support an alternate register for a summary sheet on the basis that this would seem to duplicate the provision of information in the Lessor's Disclosure Statement. It also introduces an additional register to the Torrens Register. The Committee notes that a national lease register or the Torrens Register will only provide information as to the applicable rent at the commencement of the lease and the nature of rent reviews; actual rent changes during the term of the lease, such as a result of a market review, are not captured. A lease register is often supported on the basis that it improves the general level of information about the lease for other participants in the industry. However, it is unlikely to capture all incentives and changes to rent during the lease term, which means that the information provided is of little utility.

The Committee also notes that a system of notification of retail leases to the Small Business Commissioner in Victoria under the former section 25 of the *Retail Leases Act 2003* (Vic) was abandoned in November 2012. The Committee understands that the notification system was abandoned on the basis that it imposed unnecessary costs and served no significant purpose. The Victorian experience would suggest that the adoption of a national lease register is unnecessary.

7. Full disclosure of incentives

As a general principle the Committee supports parties transacting in the market place with full information. However, the majority of the Committee regards the confidentiality of the financial arrangements between respective parties as more important than the general provision of industry information. The confidentiality of a particular incentive can benefit both parties to the lease. The majority of Committee members do not support mandating full disclosure of all incentives as it does not regard this as being in the interest of tenants or landlords.

Other members of the Committee note that it is often difficult for valuers to assess a market rent in circumstances where a lease allows a valuer to take into account incentives offered in the market using comparable data if these incentives are hidden and not available on any register which the valuer may access. Often the tenant does not have a choice but to comply with the landlord's requirement that the incentive remain hidden in a side deed. Arguably it may sometimes be in the interests of a tenant (or as the case may be, landlords) for incentives to be disclosed. Without access to the information relating to incentives, a market review may not in fact reflect the true market rent.

On a pragmatic approach, the goal of perfect information, though laudable, is most likely unachievable. Any legislative attempts to mandate full disclosure will most likely give rise to onerous prescriptive requirements which will be difficult if not impossible to enforce.

8. Provision of sales results

The Committee believes the current legislative requirements in New South Wales are working reasonably well. The collection of information regarding turnover assists in the management of shopping centres and also enables landlords to assist tenants who are struggling.

9. Contractual obligations relating to store fit-outs and refits

The Committee notes that this is an area in which disputes do arise where the information regarding fit-out and respective obligations of the parties is not well documented. The Committee does not favour highly prescriptive requirements as to what must be set out but instead suggests that education and information are key to both parties to the transaction properly documenting and fulfilling their obligations in a timely manner.

The Committee would be pleased to discuss its comments and participate further in the Inquiry. Any questions in relation to matters raised above should be directed to Gabrielle Lea, Policy Lawyer for the Committee

Yours sincerely,

Ros Everett
President