

Submission

Issues Paper - Retail and Commercial Leases Act 1995 (SA)

Property Council of Australia (SA Division)

February 2015



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Executive Summary

The Property Council of Australia extends its gratitude to Mr Alan Moss; the Small Business Commissioner, Mr John Chapman; and the Commissioner's staff for their consultative approach in undertaking a review of the *Retail and Commercial Leases Act 1995 (SA)*. We look forward to continuing to engage with you on the review process as it progresses and would welcome an opportunity to review a draft Bill once it is developed.

The Property Council is of the view that there are some ambiguities in the legislation that need to be addressed. However, the issues paper goes further than that and flags the introduction of costly red-tape for business in SA. The issues paper refers to matters raised by tenants through the Office of the Small Business Commissioner, but the Property Council of Australia notes there is no data provided in the paper on the volume and nature of these complaints. In order for regulatory burdens to be increased in this area, further evidence is required.

A full list of 41 Property Council recommendations in relation to the issues paper can be found at page 17.

Background

The economic significance of the property sector

The Property Council of Australia is the peak industry body representing property developers, property investors and South Australian businesses that provide professional services to the property industry in South Australia.

In broad economic terms the business activities of the membership of the Property Council of Australia (SA Division) represent a significant part of the South Australian economy. Their activities contribute to the following key economic outcomes:

- 6.1% of Gross State Product (\$5 billion);
- 16.1% of total State Government Revenue (\$2.5 billion); &
- 7.1% of the State workforce (58,000 jobs).

In respect to the overall state economy, the property industry is the second largest private sector employer in South Australia and overall it is the third largest private industry sector by economic output.

Property represents the physical foundation for business and job opportunities through shops, offices, industrial precincts, hotels, and public buildings, as well as places for our creative and recreational pursuits, which add so much to our quality of life. In supporting these industries, the Property Council of Australia provides a voice to ensure certainty for investment in South Australia.

General comments

The Property Council is of the view that there are some ambiguities in the legislation that need to be addressed. However, the issues paper goes further than that and flags the introduction of costly red-tape for business in SA. The issues paper refers to matters raised by tenants through the Office of the Small Business Commissioner, but the Property Council of Australia notes there is no data provided in the paper on the volume and nature of these complaints. In order for regulatory burdens to be increased in this area, further evidence is required.

Moreover, the Property Council notes that in places the discussion paper seems to be at odds with government policy around simpler regulation and removing barriers to investment in the state. It is worth noting that Point 7 of the Premier's 10 point plan for South Australia is: *South Australia, the best place to do business*. Furthermore, the actions outlined in support of the plan include:

*Create a system of regulation which promotes innovation and removes unnecessary burdens on business and the community, while safeguarding consumers and the environment.*¹

If the additional regulation proposed in the issues paper is driven by significant concerns raised by tenants through the Office of the Small Business Commissioner, evidence of the

¹<http://economic.priorities.sa.gov.au/>

nature/volume of such complaints should be made clear to justify any additional regulation in this area. The Property Council of Australia notes that it is also government policy that prior to the introduction of any additional regulation that could result in costs to business, a full regulatory impact statement be completed on those impacts in compliance with the SA government's *Better Regulation Handbook*² and that a Simpler Regulation Unit has been funded through the Department of Premier and Cabinet to implement the Premier's policy platform around simpler regulation. Moreover, the Property Council of Australia notes that there is a transparency requirement that regulatory impact statements be published online.³

The Property Council of Australia strongly supports the Premier's commitment to improving SA's attractiveness for investment and supporting economic growth through simpler regulation. A full regulatory impact statement should be undertaken on this legislation prior to its consideration by Cabinet and then Parliament. The Property Council's membership base has also indicated they would appreciate clarity on when a draft Bill will be prepared and if/when this will be consulted on.

The state of SA's economy

It is useful to reflect on the state of South Australia's economy when new regulatory burdens for business are under consideration. The decline in mining and manufacturing and a slower than anticipated international recovery in 2014 is putting increasing pressure on SA businesses; now is hardly the time to introduce more impediments to growth in the state.

As outlined in the South Australian Centre for Economic Studies' December 2014 Economic Briefing Report:

Latest annual State Accounts data indicate that the South Australian economy recorded another sub-par performance in 2013-2014. Gross State Product (GSP) – a measure of aggregate production – rose by 1.3 per cent for the year in real terms, well below the average pace of 2.4 per cent per annum over the previous decade.⁴

Furthermore:

Low rates of population growth; weak growth in domestic incomes, low consumer confidence, weak private sector investment (with the exception of housing); and continued fiscal consolidation by the Commonwealth and state governments will also serve to keep growth below its long-term trend.⁵

This is hardly an economic environment where further red-tape to business ought to be considered without a rigorous cost/benefit analysis of the consequences of such regulation.

² <http://www.dpc.sa.gov.au/sites/default/files/pubimages/documents/BetterRegHandbook.pdf>

³ <http://www.dpc.sa.gov.au/publications#regreform>

⁴ *Economic Briefing Report*, South Australian Centre for Economic Studies (December 2014) page vi.

⁵ As above note 4, page xi.

Recommendation 1: That a full regulatory impact statement (RIS) be prepared on the implications of any amendments to the legislation in consultation with the Department of Premier and Cabinet's Simpler Regulation Unit, noting Point 7 of the Premier's 10 point plan as the policy context for this RIS.

Recommendation 2: That a timeline for the review process be released with an indication of when a draft Bill will be available for public consultation.

Comments on the Issues Paper

Application of the Act

There are some significant ambiguities inherent in the legislation as it stands. For example, it is unclear whether increases in the rent threshold trigger applicability. Moreover, the regulations do not reflect the government's intention that the new rent threshold only apply to leases entered into after 4 April 2011.

Recommendation 3: That ambiguity be addressed to ensure clarity in the Act's application. The Act must also directly address what happens when rent goes over the threshold during the term of the lease.

Floor Area

The discussion paper suggests that floor area could be used to determine applicability of the Act. The Property Council of Australia strongly opposes this proposal for a number of reasons:

- Floor space is an inaccurate indicator of the value of the space. For instance, a very small retail shop in a prestigious/in-demand shopping precinct is going to attract much higher rent than a larger premises in a lower demand area. If the intent of the legislation is to address a perceived or actual inequality in bargaining power between a landlord and tenant, floor space as a threshold is at odds with the Act's intent.
- If floor area were used to determine applicability tenants could be confronted with additional costs for surveying the space. This is a new financial barrier for smaller enterprises entering into a lease for a shop or an office space, and an impediment to new businesses starting up or growing through expansion into larger retail/commercial spaces.

Recommendation 4: It is strongly recommended that rent payable continue to determine the applicability of the Act.

Rent Threshold

The Property Council is in agreement that the rent threshold not being clearly expressed as being either inclusive or exclusive of GST creates uncertainty. Furthermore, our members advise that this issue has been raised in recent times with the government when feedback on the legislation was previously sought.

Recommendation 5: That amendments confirm that the threshold is determined on GST exclusive rent payable.

Public company definition

The Property Council of Australia is in agreement that a lack of clarity around what constitutes a 'public company' creates uncertainty for parties entering into retail and commercial leases in South Australia.

The Act should not benefit private company tenants that are a subsidiary of a company headquartered overseas, e.g. huge multi-nationals. Any company entering into business in South Australia headquartered outside of Australia is likely to have significant resources compared to most Australian landlords. The act as it stands unfairly disadvantages Australian landlords over multi-national tenants.

Recommendation 6: That amendments address a lack of clarity around the definition of a 'public company.'

Changes in a company's circumstances

The Property Council of Australia agrees that the Act needs to be clarified to make it clear how it applies to a lease depending on a company's changing circumstances, for example, after a company is publicly listed.

Recommendation 7: That the Act be amended to deal with changes in a company's circumstances (for example a private company becomes publicly listed).

Section 6

Feedback from the Property Council of Australia's membership base strongly advocates for section 6 to remain as it is for the following reasons:

- It forces both parties to the table in the event of a dispute around whether a lease exists or not.
- It protects both landlords and tenants, in an instance where one party is claiming a lease doesn't exist.

- In most cases landlords and tenants have communicated to each other in writing to set out basic terms of a lease prior to possession. Section 6 means that such correspondence is considered in determining the nature of the lease.

Recommendation 8: No change to section 6.

Copy of lease to be provided at negotiation stage

The Property Council of Australia disagrees that the Act requires a landlord to provide a copy of the lease during negotiations, and notes that it actually requires a lease be **available**. An amendment to explicitly require this is not supported, for a number of reasons:

- Landlords should not be drafting an individual lease until they have fully crystallised their agreement with the tenant.
- Some landlords receive multiple enquiries regarding a potential lease, a requirement to provide a copy of the lease during the negotiation stage would be overly costly. Furthermore, this proposal could prolong the negotiation process and result in significant legal costs to both parties.

Recommendation 9: No change to the Act in terms of provision of a copy of the lease.

Disclosure statement

Feedback from Property Council of Australia members illustrates that the current disclosure statement is comparably simpler in South Australia than in other jurisdictions – providing more categories of disclosure statements would result in further compliance costs for business and confusion for both tenants and landlords.

Moreover, landlords should not be penalised through tenants failing to complete and return disclosure statements. Also, disclosure statements need to be served when a renewal of lease is entered into. As currently drafted, the Act requires a disclosure statement before the first day a renewal can be exercised, which is problematic, as the legislation should follow the business practice.

Recommendation 10: That the Act be amended to reflect business practice around the timing of disclosure statements.

Recommendation 11: That landlords not be penalised for tenants failing to complete/return disclosure statements.

Recommendation 12: That no new categories of disclosure statements be introduced.

Recommendation 13: That no penalty be introduced for the provision of an incomplete disclosure statement (noting that section 12 already provides a remedy in the case of a landlord providing information not in the form required, or false/misleading information).

Capital Expenditure

The rationale for a proposed change in this area is unclear and Property Council of Australia members advise that the Act works well in its operation in this area and aligns with taxation/accounting practices. Moreover, it is noted that if a landlord is in breach of contractual obligations regarding any capital expenditure then the tenant has a contractual remedy available to them.

Recommendation 14: No change to the Act be made regarding capital expenditure.

Lease preparation costs

The Property Council of Australia agrees that the Act should be amended to clarify what is included in 'lease preparation costs.' However, the current cap of 50% is appropriate and should not be amended.

Recommendation 15: That the Act be amended to clarify preparation costs include preparation and registration attendance costs.

Recommendation 16: That the 50% cap on costs remain.

Lease documentation

Introducing a requirement to register retail shop leases would increase costs to tenants. Most landlords allow for registration at the request of the tenant, provided their costs are paid, in any event. If this requirement were introduced, tenants would be required to pay lease registration fees and prepare survey plans. Such costs could be a real impediment to small enterprises starting up, and an additional expense for established businesses entering into new leasing arrangements. It should be noted that registration is not required in other Australian jurisdictions, so such a change would put South Australia out of step with the rest of the country and introduce additional costs to businesses.

Recommendation 17: No new requirement for retail shop leases to be registered.

Warranty of fitness for purpose

The Property Council of Australia strongly disagrees that section 18 of the legislation should be amended for a number of reasons:

- Such an amendment would make the arrangements inflexible, for instance, some tenants knowingly enter into a lease on a property

where repairs are required, as they are prepared to undertake repairs themselves in exchange for benefiting from lower rent costs.

- This proposal could potentially result in huge costs to the tenant, as rents would increase to cover the mandating of such repairs.
- Tenants and landlords are presently able to negotiate contractual arrangements that suit them relating to repairs/maintenance – removing this flexibility could be detrimental to both parties.

Recommendation 18: No change to section 18.
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Security

The proposals put forward regarding security are opposed by the Property Council of Australia for the following reasons:

- It introduces additional administrative processes for the Commissioner.
- The proposal for a four week limit on security bonds is unreasonable considering the high value of commercial leases which fall under the Act.
- The practice of seeking an additional bank guarantee is most often triggered by a landlord having a real concern about the financial viability of a proposed assignee. Restrictions in these types of arrangements will mean landlords are less likely to consent to assignments of a lease, where the assignee is less likely to meet financial obligations, which would mean fewer tenants could sell their business, which limits their options.
- Requirement to hand back a bank guarantee is most often covered by the leasing contract negotiated by the parties.

Recommendation 19: No introduction of a four week limit on security bonds.

Recommendation 20: No new restraints for requiring a bank guarantee, noting that such arrangements can be effectively dealt with by contract law.
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Term of lease and renewal

The Property Council of Australia would support an arrangement where a lawyer **or** staff member of the Small Business Commissioner's office can provide such a certificate, assuming they are appropriately qualified and trained in this area.

The five year rule is deemed as being reasonable, as beyond that there are implications for the value of the property.

Regarding section 20B(3)(b) the following words should be deleted: 'and the period of holding over is 6 months or more.'

Recommendation 21: That lawyers continue to be able to sign certificates of exclusion, and that the Small Business Commissioner also be empowered to sign certificates of exclusion.

Recommendation 22: That the following words be deleted: ‘and the period of holding over is 6 months or more’ from section 20B(3)(b).

Rules of conduct at end of term

The current arrangements regarding rules of conduct at the end of a term are reasonable and provide adequate protections for landlords and tenants for the following reasons:

- Tenancies outside of shopping centres are usually either single tenanted property or buildings with fewer than 5 tenancies. The Landlords of such properties have far less flexibility in what they can offer. To force landlords to continually re-offer the same tenancy to a tenant is unreasonable and could significantly restrict their business practices. Shopping centres on the other hand tend to be larger operations.
- Landlords who do not comply with Part 4A of the legislation are at risk of tenants holding over at their discretion.
- The purpose of the 6-12 month time frame is to provide the current tenant with ample time to negotiate a new arrangement with the Landlord, or to relocate. Tenants already benefit from 5 year terms.

Recommendation 23: That current rules of conduct at end of term remain.

Fitout

The Property Council of Australia does not agree that there is a strong rationale to introduce new definitions around fit-out, as these are commonly accepted commercial terms in usage outside of the legislation, therefore introducing definitions could make the law unnecessarily prescriptive in this area.

Recommendation 24: No amendment to section 21.

Adjustment to base rate

Again, it is unclear that there is evidence of a need to prescribe further regulation in this area. Rent reviews form commercial terms within a lease. In the case of a rent review being overlooked, tenants can benefit in that they have paid lower rent and therefore less interest in that period. Furthermore, the law already protects tenants in this area (see sections 22-23 and 35-36).

Recommendation 25: No new provisions on adjustments to base rate.

Land tax

The Property Council of Australia supports removing ambiguity in this area.

Recommendation 26: Removal of ambiguity in relation to land tax to ensure that the applicability of the Act is clear.

Outgoings

The definition of ‘accounting period’ under the Act is currently the lessors accounting period. Usually the accounting period is outlined in the lease and most often would be a calendar year or the financial year. Prescribing a definition would result in additional red-tape for businesses to comply with. The Property Council of Australia does not see from the issues paper that there is a strong case for introducing penalties in this area.

Recommendation 27: No introduction of a new ‘accounting period’ in the Act.

Recommendation 28: No introduction of a new penalty regarding outgoing obligations.

Repairs and maintenance

The Property Council of Australia strongly opposes additional regulation relating to requirements around repairs and maintenance for a number of reasons:

- Most often leases contractually require landlords to undertake repairs and maintenance.
- When a tenant is about to enter into a leasing arrangement it is up to them to inspect the premises before they sign the lease. Tenants should be free to enter into a lease where there may be some repair and maintenance issues at a lower rental rate if that is a commercially appropriate opportunity for them. For instance, a lessee may have skills in painting and may opt to do some painting of the office or shop themselves to benefit from a lower rental cost, so they can start a new business venture. Introducing additional statutory repairs and maintenance requirements on landlords will just drive up rents, which impedes business starting up and increases the costs of doing business for established enterprises.
- Furthermore, tenants are protected by section 38 of the Act if the premises is not well maintained.
- In terms of sinking funds, The Property Council of Australia is not aware of sinking funds being in common use.

Recommendation 29: No additional regulation regarding repairs and maintenance.

Lessee to be given notice

The Property Council of Australia is not aware of non-compliance issues regarding giving notice for alteration/refurbishment. Without meaningful evidence regarding non-compliance the rationale for introducing a new penalty is unfounded.

Recommendation 30: No additional penalties for landlords regarding notice for alteration/refurbishment.

Demolition

The Property Council of Australia strongly opposes the introduction of a requirement for landlords to pay for the fitout of a new premises in the case of demolition. In the case of demolition, a tenant receives six months notice and can terminate the lease at any time within that six months. This is an appropriate adjustment in favour of the tenant. To impose a requirement on landlords to pay for fit out costs in other premises is an unfair burden on business and an inhibitor to the redevelopment of property and infill development.

Recommendation 31: No change to section 39.

Damaged premises

The rationale for changes in this area is again unclear from the issues paper for a number of reasons:

- Events such as natural disasters are covered by insurance – why would the legislation need to impose another layer of regulation in this area?
- Is there sufficient evidence of landlords allowing their properties to become rundown in order to terminate a lease to trigger a regulatory response in this area? Furthermore, why would a landlord want to degrade their asset's value by allowing it to become so rundown that a tenant wishes to leave the property?

Recommendation 32: No amendment to the Act relating to damaged premises.

Consent to assignment

Assignment of a lease takes away power from a landlord to control who occupies their property. Furthermore, a landlord is already significantly restricted in the circumstances under which they can refuse a request for assignment under section 43 of the Act. If the Landlord withholds consent in breach of the Act then the tenant can litigate or enter into a dispute resolution process.

Noting that the ability to assign the lease is usually initiated by the tenant for their benefit, the rationale removing a protection regarding reasonable costs incurred by landlords from assignment is unclear (noting that premiums remain prohibited under the Act).

One concession in this area could be to reduce the 42 day period to 28 days once the landlord has been provided with all necessary information.

Recommendation 33: That the out of pocket expenses of landlords continue to be covered in the case of assignment.

Liability of lessee following assignment and lessors right to refuse sub-lease on mortgage

The Property Council of Australia has a number of significant concerns with the proposals put forward in the issues paper on sub-leasing and mortgaging.

It is a fundamental common law principle that sub-leasing does not release the tenant from their obligations. Again, it is unclear what the rationale for an amendment in this area is based upon, as no evidence has been presented on the nature or number of complaints/issues in this area

A landlord is already significantly constrained by the Act, in that it is weighted in the tenants favour if they wish to sub-let. Furthermore, sub-letting and mortgaging are very different types of arrangements and therefore should be treated differently by the legislation.

Recommendation 34: No change to the Act in relation to sub-letting and mortgaging.

Relocation

The nature of a commercial relationship between a landlord and tenant in a commercial environment means that it is in the interest of both parties to ensure that the transition to a new space goes smoothly. A tenant currently has the option to terminate the relationship if the new location does not meet their needs. There may be some situations where the new location proposed is less attractive to the tenant. If so, the tenant may negotiate lower rent. Conversely, a tenant may be offered a new location that is more desirable.

Recommendation 35: No change to the Act in relation to relocation.

Abandoned goods

Section 76 of the Act needs to be redrafted to ensure better clarity and to better protect landlords in instances where tenants have breached their lease and left a property in disrepair.

The abandoned goods provisions only apply in circumstances where a tenant has not removed their goods at the end of the lease. Landlords should not incur the expense and

inconvenience of the onerous obligations in section 76 of the Act where the tenant has breached their lease.

Recommendation 36: Amend section 76 to make it clear what ‘abandoned goods’ includes; for example, does it include fitout?

Recommendation 37: Remove overly onerous obligations on the landlord in section 76 when a tenant has breached their lease.

Main issues not covered by the Act

Termination

The issues paper implies that terminating a lease is a complex and expensive process, which is not the case. A lease can be terminated through serving a notice of termination. The process around notice for breaches and providing a reasonable time to remedy a breach is covered in existing legislation *Landlord and Tenant Act 1936* (SA). Again, a case for amending the legislation in this area has not been made clear in the issues paper.

Recommendation 38: No new termination provisions, noting that this is already covered by legislation.

Condition reports

The additional burden on landlords and tenants around a new legislative requirement to complete condition reports is an unreasonable impost on business and not supported by The Property Council of Australia.

Recommendation 39: No new legislative requirement for condition reports.

Lease Documentation

The Property Council of Australia does not support a mandated pro-forma lease, however, would not oppose the Office of the Small Business Commissioner providing a non-mandatory lease template for those requiring assistance in preparing/negotiating a lease.

Recommendation 40: A non-mandatory lease template available through the Commissioner’s office is supported.

Dispute monetary limits

The Property Council of Australia agrees that clarity should be provided around the monetary limit for matters the Commissioner may mediate.

Recommendation 41: The Property Council of Australia supports the introduction of a monetary limit of \$100,000 for mediation by the Commissioner.

Full list of recommendations

Recommendation 1: That a full regulatory impact statement (RIS) be prepared on the implications of any amendments to the legislation in consultation with the Department of Premier and Cabinet's Simpler Regulation Unit, noting Point 7 of the Premier's 10 point plan as the policy context for this RIS.

Recommendation 2: That a timeline for the review process be released with an indication of when a draft Bill will be available for public consultation.

Recommendation 3: That ambiguity be addressed to ensure clarity in the Act's application. The Act must also directly address what happens when rent goes over the threshold during the term of the lease.

Recommendation 4: It is strongly recommended that rent payable continue to determine the applicability of the Act.

Recommendation 5: That amendments confirm that the threshold is determined on GST exclusive rent payable.

Recommendation 6: That amendments address a lack of clarity around the definition of a 'public company.'

Recommendation 7: That the Act be amended to deal with changes in a company's circumstances (for example a private company becomes publicly listed).

Recommendation 8: No change to section 6.

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Recommendation 14: No change to the Act be made regarding capital expenditure.

Recommendation 15: That the Act be amended to clarify preparation costs include preparation and registration attendance costs.

Recommendation 16: That the 50% cap on costs remain.

Recommendation 17: No new requirement for retail shop leases to be registered.

Recommendation 18: No change to section 18.

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Recommendation 23: That current rules of conduct at end of term remain.

Recommendation 24: No amendment to section 21.

Recommendation 25: No new provisions on adjustments to base rate

Recommendation 26: Removal of ambiguity in relation to land tax to ensure that the applicability of the Act is clear.

Recommendation 27: No introduction of a new 'accounting period' in the Act.

Recommendation 28: No introduction of a new penalty regarding outgoings obligations.

Recommendation 29: No additional regulation regarding repairs and maintenance.

Recommendation 30: No additional penalties for landlords regarding notice for alteration/refurbishment.

Recommendation 31: No change to section 39.

Recommendation 32: No amendment to the Act relating to damaged premises.

Recommendation 33: That the out of pocket expenses of landlords continue to be covered in the case of assignment.

Recommendation 34: No change to the Act in relation to sub-letting and mortgaging.

Recommendation 35: No change to the Act in relation to relocation.

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Recommendation 41: The Property Council of Australia supports the introduction of a monetary limit of \$100,000 for mediation by the Commissioner.