

COMMERCIAL TENANCY (RETAIL SHOPS) AGREEMENTS AMENDMENT BILL

Second Reading

MR SHAVE (Alfred Cove - Minister for Fair Trading) [11.40 am]: I move -

That the Bill be now read a second time.

The Commercial Tenancy (Retail Shops) Agreements Act regulates lease agreements for certain small businesses conducting their operations in retail premises of 1 000 square metres or less. The Act provides for the determination of questions arising from all matters associated with the lease and dealings between the tenant and landlord. Its main aim is to improve the parties' understanding of their rights and responsibilities involved when entering a retail leasing contract. It also provides relatively inexpensive and practical procedures for resolving conflicts about these matters.

In completing a statutory review of the Act, I am proposing amendments that represent outcomes from an extensive consultation process. The Green Bill issued by the Government late last year gave all stakeholders from the retail sector and property industry the opportunity to consider a range of proposals. These proposals did not represent the settled position of the Government. They were understood to represent a set of reforms accumulated from previous reviews and desired by the industry to enhance the purpose of the Act.

Following a formal public submission period of five months, discussions have continued with peak industry groups and interested individuals to clarify the impact of a wide range of proposals. The amendment Bill is an amalgam of a number of these proposals, including refinements, additions to and deletions from the original Green Bill.

The amendment Bill upholds a number of parameters. Firstly, in regulating the activities of parties involved in commercial retail leases, the new measures do not intend to apply overly prescriptive procedures in these transactions. However, the review has identified that, due to a changing environment, some fine tuning of the Act is required. Secondly, the Bill's initiatives are directed largely to new leases only, with no retrospective application to current leases. The amendment Bill also contains improvements in drafting aimed at overcoming difficulties that have been experienced in the interpretation and administration of the Act. In addition, the amendments reflect changes to the retail industry environment since the Act commenced in 1985 and the most recent 1990 amendments were introduced. The proposed amendments also deliver on the Government's stated commitment to provide a more secure environment for traders; encourage landlords to make agreements which suit the dynamics of the individual properties concerned and the specific retail businesses that are being accommodated; and place a greater emphasis on disclosure of all conditions and obligations.

The main elements in the amendment Bill deal with reviews of a tenant's rent, valid occupancy cost contributions, and the disclosure of all pertinent information prior to the lease contract and protective audit provisions. Specifically, these deal with interpretations of major terms underpinning the amendments. These include refinements to "retail shop lease" and "shopping centre" to allow for associated open space used for retail purposes and includes multi level and strata developments. The term "total lettable area" is defined as the aggregate of the retail floor areas, the latter term being added to uniquely identify leased space subject to the Bill. When combined, both terms determine the relevant proportion for cost apportionment to the retail tenant.

A tenant guide will be introduced for enhanced disclosure and tenant education. The tenant guide will address a range of rights and obligations for landlords and tenants. Essentially the guide will be a plain language explanation of key principles contained within the amended Act. In particular, it will include details of tenants' rights in respect of void clauses such as the insertion of prescriptive trading hours arrangements in leases. The tenant guide will also recognise the practice of some clauses, which do not apply to leases covered by the Act, being used as a means of misleading tenants with regard to their rights. The guide will recognise the legal realities and resulting difficulties if these provisions were to be prohibited outright. The guide will be developed in conjunction with an industry reference group and be prescribed in regulations to support the amended Act. Sanctions will be imposed if this guide is not provided.

The Government believes that it is unfair for assignors to be required to guarantee the performance of the ingoing assignee over the balance of the lease term. Accordingly, the amendments aim to remove any doubt that once an assignment of a retail shop lease under the jurisdiction of this Act has occurred, the liability of the assignor tenant or his or her guarantor will end in respect of the new business occupancy. Any moneys owed by the outgoing tenant will be his or her responsibility.

The Bill ensures that only one means of calculating rent per review will be specified in a lease. When calculating rent due at a rent review, some leases feature more than one method of calculating rent, such as being the greater of CPI, market rent, or 10 per cent. Further provisions also allow rent only to increase, even when market conditions at the time of the review should see a decrease in the rent. The amendments will require that for new leases, prior to agreements being finalised, the single basis on which rent reviews will be conducted must be clearly disclosed. The amendments also confirm the Government's contention that for new lease agreements, the market rent will be able to increase and decrease to reflect market conditions prevailing at the time of the review.

The Bill also clarifies beyond doubt that "ratchet clauses" which ensure that rents can only increase on review are prohibited. In the assessment of what constitutes market rent, the valuer will be required to adopt proper land valuation practices. These standards are currently being developed by the valuation industry and will be referred to in the regulations supporting the Act.

The Bill provides that either party to the retail lease may initiate a rent review action. In the absence of specific timing on this issue there is a default timetable to initiate the review not earlier than three months prior to or not later than six months after the scheduled review date. This will work to protect the tenant's rights to take advantage of market conditions rather than for only the landlord to have this ability. For all leases, in cases of dispute, the existing rent will continue until the new rent is determined. When the new rent level is decided, any adjustment in favour of the landlord or tenant will rank equally with all other lease commitments and be due and payable with the next invoice.

The registrar's powers to determine rent reviews are also confirmed by the Bill together with the ability of the registrar to call for mandatory disclosure of valuation evidence from the parties. These provisions will apply to all leases. With regard to contributions to landlord expenses, the Bill requires that a retail lease seeking the recovery of operating expenses from retail tenants will specify how the amount claimed has been calculated, apportioned and is to be paid by the tenants. This clause will include retail premises whether as stand alone shops, strata developments, or shopping centres comprising one or more buildings or a cluster of five or more retail shops.

The relevant proportion principle is introduced by the Bill to set an upper limit to the amount tenants can reasonably be asked to contribute to the landlord's operating expenses in running a shopping centre. Some industry practices have seen major tenants being given significant discounts by landlords on a shopping centre's operating expenses. In order to overcome any shortfall from these negotiations, in some instances landlords have then allocated these shortfalls to other tenants, generally the smaller specialty retailers, in the centre. In addition, some shopping centres ownerships with vacant shops have loaded up their tenants with the expenses which should have been allocated to the vacant shops. Practices of this nature are patently unfair. As these costs are unrecoverable, the landlord, in the absence of tenants in these vacant shops, should bear these costs.

The proposed amendments therefore limit a tenant's contribution to all valid operating expenses such as rates and

taxes, insurances, cleaning and the like by relating the amounts they contribute to the proportion which the floor area of the tenant's shop bears to the shopping centre's total lettable area. The clear intention is to ensure that small tenants do not contribute to expenses that are not applicable to their tenancy. The Government is not, however, precluding any negotiated agreement between the parties that provides for a contribution by the tenant of less than the relevant proportion.

With regard to disclosure and audit requirements for a shopping centre's operating expenses, the Bill's provisions have been expanded to allow greater scrutiny of the landlord's charges. These changes have been endorsed by the Joint Legislation Review Committee of the peak audit industry group and are aligned with similar provisions in other States.

These provisions also ensure that parties pay only their fair share by specifying that tenant contributions to landlord expenses will be limited to the tenant's proportion of the total lettable area of the shopping centre. To complement this disclosure between the parties to a lease, the Act will also require that the centre's total lettable area, and any changes in the year, be verified by a registered company auditor during the conduct of the audit.

In recognition that both landlords and tenants will benefit from these audited provisions, the auditing costs will be equally divided between these parties. However, there will be no need to conduct an audit where recoveries are limited and these expenses are readily verifiable and copies of the charges are supplied. This would include simple lease agreements where rates, taxes and insurances expenses are the only recoveries outside of rent payments. In addition, to ensure compliance by the landlord, provision is made that tenants will not have to pay the current year's operating expenses if the previous year's audited accounts have not been supplied after three months.

The Bill also acknowledges that certain expenses can be attributable to a particular tenant or group of tenants. These referable expenses are usually outside the normal common operating expenses budget and are the result of additional service requirements, such as extra cleaning and disposal of food waste.

Landlords will be prevented from recovering management fees directly from tenants. There are strong differences in the debate on the legitimacy of tenants paying the management fees directly to the managers. Tenants argue that although they pay the fees, they are not a party to the agency contract and have no say in the selection and performance of managers. Additionally, if landlords were directly responsible for remunerating their managers, they would take a greater interest in supervising their activities to ensure the highest standards of performance at the best price.

On balance, the Government has agreed with these arguments and has defined management fees within the Bill to give effect to this decision. This measure will apply to new leases and ensure that responsibility for the supervision of shopping centre management is undertaken by the parties who are responsible for the appointments to the management-related positions in a shopping centre.

The issue of tenant contributions to the landlord's land tax assessment has been contentious. Comment provided during the Green Bill consultation phase revealed that where disputes occurred, they related to inappropriate charges being claimed by the property ownership. To reflect fairness and essentially commercial practices in this matter, the proposed amendments will ensure the tenant pays only the amount relevant to his or her retail outlet by prescribing that the contribution will be limited to the "notional land tax". This amount is calculated on the basis that the land on which the tax is assessed is the only land owned by the landlord and does not attract tax at the higher multi-ownership rate.

The area of sinking funds has also seen conflict between landlords and tenants. Restrictions which limit the use of these funds to future repairs and maintenance and non-capital works initiatives will remain. The proposed amendments will require that any other sinking funds are used only for the specific purpose for which they are created. Moneys in these funds are maintained for the benefit of the shopping centre and are clearly not for any other uses. The amendment Bill extends the protection of the sinking funds provisions to all other funds and reserves to which the retail tenant contributes. This will include the audit of promotion funds and marketing levies.

Two further issues in retail leasing agreements are also included in the legislation, these being the choice of trading hours by retail tenants and the determination of certain costs of occupancy with strata title centres. As a matter of principle, the Government believes tenants have the right to determine their trading hours to satisfy the needs of their business, their marketing environment and their personal circumstances. The Government's position is to allow tenants complete discretion to determine their own trading hours. This is consistent with the current conditions set by section 16 of the Retail Trading Hours Act. This measure supports that position and ensures that any specification of trading hours in a lease is void.

Additional protection is to be extended where a tenant's lease is not renewed for the specific reason that the lessee does not open at the hours specified by the landlord. Here, the tenant can apply to the registrar and Commercial

Tribunal for compensation. The tenant guide in support of the Act will also deal with this initiative.

An anomaly has been identified in the Act regarding strata title levies. Strata levy fees may include more items and charges than allowed under the Bill, which deals with valid contributions to landlord expenses. In the past, the Commercial Tribunal has ruled that landlords cannot recover any strata title levies, but this interpretation was never intended by the Act. There are serious financial implications for landlords in these circumstances if they are unable to recover levies as legitimate expenses.

As a consequence, appropriate amendments to address these issues are featured in the amendment Bill. The amendments will allow strata title levies to be included as a contribution to landlords' expenses, provided these expenses comply with existing provisions of the Act. Non-operating expense items such as capital works, construction, extensions or plant and equipment replacement and upgrades will continue to be disallowed, as is the current situation.

Generally speaking, the amendments will apply upon proclamation in respect of the definitions, the powers of the Commercial Tribunal and its registrar, confirmation that tenants can have their choice of hours of operation and strata title levies. It will apply from 1 July in the 1998-99 financial year or the next applicable accounting year in respect of the auditing of expenditure and allocation of associated costs, the auditing of sinking funds and all other contribution funds.

Importantly, the amendments which rely on the concepts of relevant proportion and total lettable area will apply to all new leases and extensions of existing leases. The Government acknowledges the primacy of contracts and does not therefore seek to retrospectively change existing commercial arrangements.

The amendments will make a significant contribution to the Government's aim of making the Western Australian marketplace fairer, more competitive and better informed. The measures also address the concerns raised by industry stakeholders during the extensive consultation processes, and which were reinforced at the national level, about the need for improved retail legislation. The Commonwealth Government has recently announced a series of principles to promote fair competition and the protection of the small business sector. The full details and impact of this initiative are presently being formulated.

Together with my ministerial counterparts from other States, I will meet with the Commonwealth in December to further develop a set of nationally consistent principles for the protection of small retail business tenants. Although these amendments are consistent with that approach, further changes could possibly be introduced. However, the State Government's view is that the local retail industry needs to benefit from the findings of the completed consultation process rather than deferring in favour of the prospect of further possible improvements in retail leasing legislation. I commend the Bill to the House.

Debate adjourned, on motion by Mr Cunningham.