RETAIL LEASES AMENDMENT (REVIEW) BILL 2016

First Reading

Bill introduced on motion by Mr John Barilaro, read a first time and printed.

Second Reading

Mr JOHN BARILARO (Monaro—Minister for Regional Development, Minister for Skills, and Minister for Small Business) (16:32): I move:

That this bill be now read a second time.

I start by recognising Robyn Hobbs, OAM, the NSW Small Business Commissioner, Candace, Nicola and Alex, and the rest of the team from the Office of the Small Business Commissioner, and thank them for their work in reviewing the Act and bringing the Retail Leases Amendment (Review) Bill 2016 to the House. The workload over the past couple of years has been significant and their effort must be acknowledged. The bill amends the Retail Leases Act 1994. These amendments will ensure the Act increases transparency and certainty in the New South Wales retail leasing sector. The amendments will improve standards of conduct between the parties to a retail lease, as well as increase the operational efficiency of the Act by simplifying its key processes.

The Retail Leases Act 1994 was introduced to help level the playing field between tenants and landlords of retail shop leases. It was a significant reform to safeguard the rights of parties to retail tenancy agreements. We know the ability for a tenant to strike an agreement with a landlord on a fair basis is the cornerstone of any successful retail business. At the core of the Act is a dispute resolution mechanism to help parties resolve the vast majority of their disputes without having to go to court. As we all know, the cost of litigation is prohibitive for small businesses, and an important business relationship will not survive a dispute that leads to litigation or indeed a court battle. The protective measures of the Act apply equally to both retailers and landlords, as many landlords are also small business owners.

Now, more than 20 years later, we find that the combination of having a legislative framework and the provision of free strategic and procedural advice with a low-cost mediation service offered by the New South Wales Small Business Commissioner has been a resounding success. The Act is a testament to the foresight of those who pushed the first bill in 1994. It was the Hon. Ray Chappell, Minister for Small Business and Regional Development and Nationals member for Northern Tablelands, who had the vision and foresight to introduce the bill into Parliament. In 1994, as now, the Government was reluctant to interfere in commercial dealings by introducing legislation. Today, our objective remains the same: to foster good leasing practices in the retail industry—nothing more and nothing less.

The retail market contributes significantly to the New South Wales economy. According to Australian Bureau of Statistics data there are more than 44,500 retail businesses in New South Wales. The retail industry accounts for almost 390,000 jobs and $36 billion dollars in annual sales. Eighty per cent of retail leases in New South Wales are located outside shopping centres, whilst 20 per cent are within shopping centres. Ninety-six per cent of retailers are small businesses with fewer than 20 employees. Small businesses are indeed the heartbeat of the New South Wales economy, and to support the growth and sustainability of the retail industry we must ensure that the protective measures of the Act remain relevant. The Act must be amended to respond to the needs of an industry that is undergoing rapid and significant change. Today, I come to the House with arguably the most progressive and balanced retail leases Act review in Australia—one that increases transparency, provides equity and certainty, removes Government red tape, makes it easier to do business in New South Wales, and adapts to a digital way of doing business.

I am also pleased to update the House on an industry first development. The major retail industry stakeholders have reached agreement without the heavy hand of Government on a voluntary code of conduct, which we will call "the code". As part of the final consultation process the Shopping Centre Council of Australia, National Retail Association, Australian Retail Association, Franchise Council of Australia and the Pharmacy Guild of Australia have developed this voluntary code of conduct to address a number of concerns identified over the course of the review. The code addresses the reporting of sales data and occupancy costs and increased transparency in the lease negotiation process, and seeks to level the playing field between landlords and retailers through mutual obligation. It is an industry-led solution that addresses one of the most contentious aspects of the shopping centre landlord-tenant relationship—turnover data. I am pleased to learn that there are a number of specialist retailer groups seeking to enter into the code.

The Retail Leases Amendment (Review) Bill 2016 will reform the Retail Leases Act 1994 to ensure it remains consistent with the changing needs of the industry. The bill takes a practical approach to the inevitable tensions between the needs of landlords and of , and the commercial rights. The bill will amend the Act to increase transparency and certainty between the parties during the negotiation stage. It ensures that landlords must disclose certain costs in some detail before the tenant is bound to the lease. The bill will improve access to justice and remedies by increasing the financial jurisdiction of the NSW Civil and Administrative Tribunal [NCAT] to deal with a greater number of matters, and empowering NCAT to award compensation to a party that suffers harm as a result of breaches of some new provisions of the Act by their counterpart to a retail lease. The bill will increase operational efficiency by simplifying the process of starting or transferring a retail lease, and it repeals unnecessary provisions and makes various technical amendments to improve the operation of the Act.

The bill makes amendments to clarify the landlord's disclosure obligations. All landlords will know what needs to be disclosed, and tenants will understand what they are committing to before being legally bound to a lease. The Government is committed to ensuring Parliament's original intent for upfront disclosure of the financial cost of the lease should be mandated as a foundation of the Act. An inability for retailers to plan their businesses and manage cash flows greatly increases the chance of failure, particularly for small businesses. Incomplete or inaccurate disclosure is a source of a substantial number of disputes; the actual amount charged for outgoings can vary substantially from the estimates provided. The disclosure obligation in the Act when interpreted by NCAT identified a loophole that has allowed for an imbalance between landlords and tenants in leasing agreements. The bill clarifies the obligation for landlords to disclose certain terms of the lease at least seven days before a tenant is committed to a lease.

The amendments make it clear that tenants are not liable for undisclosed outgoings other than an outgoing in the nature of a tax, rate or levy that is imposed by any Act after the lessor's disclosure statement if given. Advertising and promotion costs are not outgoings for this purpose. The bill legislates that if the lessor's disclosure statement provides an estimate of the amount of an outgoing and there was no reasonable basis for the estimate, the tenant's liability for the outgoing will be limited to the estimated amount.

Future increases in the outgoing will be limited by reference to the estimated amount—for example, the cost from the previous year. To illustrate what this means, imagine the landlord estimates that a tenant's contribution for land tax will be $1,000 per quarter but the actual cost is $2,000. This represents a variation of 100 per cent. Therefore, the tenant will be liable for only 50 per cent of the actual amount of the outgoing throughout the term of the lease.

A breach by a landlord to disclose outgoings is dealt with by reducing the tenant's liability for outgoings. When there are other breaches to the disclosure obligations, such as a failure to disclose when the lease for the anchor tenant expires, the NSW Civil and Administrative Tribunal [NCAT] can award compensation to put the tenant back into the position in which they would have been if proper disclosure had been made. Under the current Act, landlords are able to recover non-disclosed outgoings and potentially charge a higher rent than if the tenant factored in the actual cost of outgoings. A tenant's only alternative for improper disclosure in the current Act is to walk away from

the lease—and all their sunk investment within the first six months. In fact, if a tenant walks away the landlord benefits from the fit-out work, which has been funded by the tenant, as they can charge a new tenant a higher rent. Without compensating the tenant for their lost investment, such as for expensive fit-outs, the current remedy is inadequate.

The amendments allows the NCAT to rectify a lease or lessor's disclosure statement to correct an error or omission, giving effect to the intention of the parties when the lease was entered into, or to reflect the actual disclosure of information between the parties if the disclosure requirements of the Act are otherwise met. This is particularly important if the landlord sells the building or if the tenant sells the business and the new party does not know the original deal that was struck. These changes are consistent with the Act's objective of ensuring that parties enter into a lease from the best possible negotiation position—with certainty, and the information necessary to make effective business decisions. These reforms provide incentives for landlords to share the important information they hold, and for disclosure statements to be accurate. This change will minimise disputes over outgoings and the detriment caused to tenants, who are liable for costs for which they have not been able to properly budget. These amendments are consistent with a key recommendation in the 2008 Productivity Commission's report to encourage transparency in dealings between landlords and tenants.

One of the principal imbalances between landlords and retail tenants during negotiations relates to market information. This includes access to information about the value of leases in the market, the turnover a lease is likely to produce, and the landlord's collection and use of tenant's turnover figures. The result of this imbalance is that tenants feel landlords hold all the important industry information and tenants are unable to compete on a level playing field. As a result of this review, those involved in the industry have worked together and an outcome has been achieved to increase access to market information. I commend the Australian Retailers Association, the National Retail Association, the Pharmacy Guild of Australia, the Franchise Council and the Shopping Centre Council of Australia for having reached agreement on a voluntary Retail Industry Code of Practice—the Reporting of Sales and Occupancy Costs. This code is an agreement on the collection and sharing of industry information. There is an implicit duty of good faith within the code and those associations are now working together in a collaborative way. Consistent with New South Wales Government's objective of letting industry develop its own solutions to issues, those parties have found consensus on issues that have been previously unworkable.

The code will support enhanced competition for retailing space and more market-based outcomes from rent negotiations. The bill recognises that retail is a dynamic industry and, as shopping is moving online, that there is a shift in the way the industry operates. Some tenants are required to report their turnover. That can be a significant issue when a sale comes through an online portal. The bill provides that a tenant cannot be required to provide the landlord with information about online transactions, except for transactions where goods or services are delivered or provided from, or at, the retail shop or retail shopping centre in which the shop is located, or where the transaction takes place while the customer is at the retail shop. Additionally, the bill provides that for the purposes of determination of rent by reference to turnover, turnover does not include information about online transactions other than transactions where goods or services are delivered or provided from, or at, the retail shop or retail shopping centre in which the shop is located, or where the transaction takes place while the customer is at the retail shop. For example, if a customer is in a store and uses a store device to customise a product before ordering, turnover information can be collected by the landlord.

Turning from the proposals that increase transparency, I will now outline the second area of amendments. The bill amends the financial jurisdiction of NCAT to increase it from $400,000 to $750,000. This acknowledges increases in the cost of leasing and, coupled with a broader range of remedies, will improve access to justice by enabling NCAT to deal with a greater number of matters. As the majority of disputes are settled through mediation, it is unlikely that the amendments will produce any long-term increase in litigation. The final amendments in the bill relate to increasing the operational efficiency of the Act by streamlining processes, repealing unnecessary provisions and effecting various technical amendments. The bill consolidates and streamlines provisions relating to the process for obtaining a landlord's consent to assign a lease. The amendments remove confusion

by separating the processes for assignment from the process for obtaining protection from any ongoing liability after a lease has been transferred. The current Act is not sufficiently clear on the assignment requirements. The amendments to the Act simplify the assignment provisions to enable tenants to transfer the lease and/or sell their business while ensuring the landlord gets a new tenant that meets the landlord's tenancy requirements. Under the current system, landlords can decide what type of tenant they require. They can require that a certain level of capital is available or that a certain level of retailing experience exists. The shop cannot be passed on to someone with less experience or financial resources without the landlord's express consent.

The bill amends the Act to make it clear that the point in time when a proposed assignee's financial resources and retailing will be assessed against those of the tenant is at the time the lease is assigned. This amendment—because it will lower the standard that the landlord can hold the new tenant to when assessing whether to consent to an assignment—will assist tenants who want to sell a business that is not doing well. This will assist tenants to assign their leases when retail businesses are sold on retail strips where there are high vacancy rates. Conversely, if a landlord is willing to take a punt on someone just starting out, who later becomes a success, they will not be compelled to consent to an assignment to a tenant with unproven skills like those of the proposed assignor at the beginning of their lease. Whether it is more or less advantageous to a landlord for a tenant to be assessed at the beginning or the end of the relationship will depend on the landlord's circumstances and the skills and financial resources of the tenant who wishes to assign their lease. In addition, particular locations, especially those with public significance, bring complexity to the issue of assignment.

There are instances in which a tender process may require a security clearance to ensure that a tenant is considered as a fit and proper person, and any other issues may weigh heavily on a public tendering process. The amendments recognise that a landlord may impose those types of requirements for employees of a retail shop, and that landlords who award leases by a public tender process may require any proposed tenant to be held to the same criteria. The bill will also introduce the requirement for landlords to register leases for a term of more than three years, and for a tenant to be provided with an executed copy of the lease. The time for registration has been extended to three months after the tenant has executed and returned the lease to the landlord because having a lease with multiple landlords and a mortgagor is not always a simple process. Lease registration provides a fundamental protection for a tenant's investment in a retail business against transfers in the ownership of the building. Failure to register a lease greatly weakens the position of retail tenants if a landlord sells the premises or a mortgagee takes possession of the property. Industry stakeholders have raised concerns regarding hundreds of unregistered leases in major suburban and regional shopping centres.

The bill introduces a requirement for a copy of the executed lease to be provided to a tenant within three months of the tenant providing an executed copy to the landlord or landlord's agent. Tenants are disadvantaged when they are denied a copy of the lease, which is required by franchisors or a lending facility to secure finance. The largely unregulated nature of bank guarantees has resulted in poor practice among some landlords and agents. At the end of a lease, by delaying the return of a bank guarantee document, landlords can limit a tenant's ability to raise capital to finance a new business or to move to a new location.

This happens by simply holding on to the document that is a bank's commitment to unquestioningly provide a tenant's funds on demand. Bank guarantees have been used by some unscrupulous landlords as leverage to pressure a tenant into settling a dispute and accepting a less favourable outcome. Others have drawn down on bank guarantees for illegitimate purposes unrelated to a tenant's performance of obligations under a lease, such as the landlord's own cash flow problems. At other times, the return of a piece of paper is just not a priority for an agent or landlord who is possibly annoyed that the tenant found another shop to rent.

Seeking an order from NCAT for the landlord's use of a bank guarantee for an illegitimate purpose is a costly exercise that is a difficult option for most tenants. Landlords, who fail to return a bank guarantee within two months of a tenant completing performance of their obligations under a

lease, will be subject to a penalty and NCAT may make an order to return funds they are not entitled to keep. One of the key recommendations in the 2008 Productivity Commission report was that clear requirements for bank guarantees should be established to improve transparency and certainty in retail lease relationships. The bill clarifies when demolition clauses can be triggered. This addresses landlords' uncertainty as to when their use is legitimate. Demolition clauses in leases require a tenant to vacate the premises so that the demolition of a substantial part of the building can take place.

The Act currently provides lessee protections for termination of a lease where the landlord proposes to demolish a building. The amendments clarify when demolition clauses can be triggered by taking out the word "substantial". Termination on the grounds of proposed demolition is only permissible when the shop requires vacant possession. The bill's amendment will eliminate concern that a landlord cannot use a demolition clause unless the whole building is being demolished, yet prevent the use of demolition clauses to terminate a tenant's business for an illegitimate purpose. Demolition clauses are frequently used to change tenancy mixes and deny tenants their property rights in favour of another tenant. When used unjustly, it means a landlord can use a demolition clause as a trigger to terminate a lease if a tenant offering a higher rent wants the tenant's shop, yet the tenant is committed to a lease agreement for three to six years with no ability to terminate the lease, regardless of how things are going.

The bill also makes a number of amendments to clarify provisions in the Act that have been the source of disputes over differing interpretations. The amendments clarify when leases in an office tower will come under the operation of the Act by removing an exception from the Act for premises in an office tower that forms part of a retail shopping centre. This has been repealed on the basis that the exception is unnecessary because an office tower does not form part of a retail shopping centre merely because it is in the same building as, or is above, the retail shopping centre. A food court or shopping precinct of an office tower is capable of being separately distinguished from the office tower for the purpose of the operation of the Act. This change is certainly not intended to capture non-retail uses in an office tower.

The bill also makes it clear that a landlord cannot recover from a tenant the cost of obtaining a mortgagee's consent to a lease. There are a number of amendments to operational provisions to enable the transition of the Retail Bond Scheme as part of a new digital platform with a contract management system and secure escrow holding service. This is a very exciting development we will learn more about in early 2017. The bill repeals the minimum five-year term for retail leases, transfers the administrative process for the appointment of specialist retail valuers to determine rent disputes from NCAT to the Registrar, and repeals redundant references to stamp duty. The Government is committed to reducing red tape for industry. By repealing the minimum five-year term, streamlining assignment and disclosure processes and clarifying provisions, the New South Wales Government is reducing red tape for the retail leasing industry.

The Government has undertaken an extensive period of consultation on the amendments. The amendments represent the outcome of the most substantive review of the Act since it was introduced in 1994. The bill introduces amendments that were put forward by the industry and developed through a lengthy and multi-tiered consultation process. Following the consultation period, the Office of the NSW Small Business Commissioner has engaged extensively with industry and government stakeholders to determine sensitivities and test recommendations. The bill's proposed amendments have been developed in conjunction with stakeholders in the sector.

As mentioned earlier, the major industry associations, the national Australian Retail Association, Pharmacy Guild of Australia, the Australian Retailers Association and the Shopping Centre Council of Australia have been actively involved in the process on particular points concerning leases in shopping centres. Some amendments have not progressed due to the lack of consensus among the major stakeholders representing large landlords and retailers in large shopping centres. Industry associations support the amendments to the Act that relate to their members. As the Minister for Small Business I have protected the key amendments that are needed to allow small business operators, be they landlords or tenants, to make and keep their deals as leases are the lifeblood of

the retail leasing industry. In summary, this bill introduces important reforms to support the future of small businesses in the retail industry. I commend the bill to the House.

Debate adjourned.