

# HERRO SOLICITORS

Level 4, 234 George Street Sydney NSW 2000 | GPO Box 4334 Sydney NSW 2001

DX 10194 Sydney Stock Exchange NSW | Tel: +612 9247 0100 | Fax: +612 9247 0700 | www.herro.com.au

---

## **Inquiry into the Market for Retail Tenancy Leases in Australia**

I am Principal Solicitor of Herro Solicitors, a Sydney based law firm that specialises in retail leasing. I was admitted into practice as a Solicitor in 1987. I had also been managing director of a chain of retail stores for twelve (12) years. I am an Accredited Mediator and am involved in mediation of retail lease disputes, both in the capacity of advocate and mediator. As a Solicitor, I predominantly represent tenants and also represent some landlords.

### **1. What are the strengths and weaknesses of the current structure and functioning of the Retail Tenancy Market?**

1.1 I have been unable to locate, prior to the date required for submission, statistics to confirm the statement I am about to make, but would suggest that it would assist the Commission if data could be obtained that would graph retail sales against occupancy cost for specialty retailers in shopping centres over the past twenty (20) years. From my experience, the growth in rental/occupancy costs has far exceeded the growth in sales for specialty retailers over this timeframe.

1.2 The greatest concern in the area of retail leasing is the imbalance of market power of the shopping centre. To site a typical example. A retailer may open a store in a regional shopping centre and obtain a five (5) year lease. The retailer is required to fitout the premises and pay for many other expenses which prior to the evolution of large shopping centres, used to be considered the responsibility of the landlord but which now have been shifted to the tenant. Towards the end of this five (5) year period an offer for lease may be made to the tenant by the landlord. It is rare that a retailer is provided with an option in large shopping centres. At this time the tenant is in a considerably weaker bargaining position. The tenant has expended capital and energy in building his or her business and establishing goodwill but without a lease this goodwill is almost worthless. This places the shopping centre owners in a strong bargaining position - the value (and sometimes the future existence of the business) depends on the grant of a lease.) At this time a shopping centre landlord, if it wishes to grant the tenant a further lease will require the tenant to refit the store and the shopping centre landlord will invariably increase the rent. (It may assist the Commission if it could obtain statistics as to the average rental increase for specialty shop retailers at the time of renegotiation or exercise of option.) In my experience the rent is almost always raised far in excess of the increase in sales. The problem lies in what choices does the tenant have if the rental increase is unreasonable or almost unsustainable? There are now very few viable strip shopping centres in Sydney. In the Sydney CBD, the one shopping centre owner controls many of the shopping centres. In most suburbs where there is a regional shopping centre, that regional shopping centre already contains the mix of major retailers, for example Myer or David Jones, the discount retailers for example Kmart and/or Target and the supermarket chains whether Coles or Woolworths and other discount retailers, so that opening of a

second shopping centre is simply not viable. The zoning may not permit another shopping centre to be built in that suburb. Further would it even be possible to obtain another site in that suburb that would be able to cater for an entire new shopping centre? The market is probably already saturated. There are only limited types of retail stores which can survive on strip shopping centres in light of the importance of obtaining the right mix of retailers for a shopping centre to be viable. In this case if the shopping centre landlord asks for an unreasonable increase in rent, where can the tenant seek an alternative? This is the fundamental problem experienced by retailers. The question really becomes whether the tenant wants to continue to be in business or not. Is the tenant prepared to forego its goodwill and the business become almost worthless? It is not uncommon in these circumstances for a tenant to feel they have no alternatives but to execute the lease and hope to increase sales. The unfortunate reality is that during the further terms tenant cannot meet their commitments. Unfortunately what avenues of assistance are open to the tenant? Governments (both Federal and State) must consider the reality of the tenant's position due to the monopoly of the large shopping centre. If we are to maintain a competitive and sustainable retail environment for tenants, government must intervene to alleviate the monopolistic bargaining position of the landlord. If one reads finding number 12 of the General Purpose Standing Committee Parliamentary Inquiry of the New South Wales State Legislative Council being report 11 dated December 2004 into the Designer Outlet Centre, Liverpool - Orange Grove, one has reason to be concerned. Tenants represent a significant part of the Australian public. I sincerely believe that there is a significant injustice to specialty retailers in this country and this imbalance needs to be addressed. This should be a goal of both Federal and State Governments. Otherwise, it will mean that the valuable contribution made by smaller retailers will not be sustainable in the long run. Ideally, it would be an achievement if shopping centre owners realised this obligation themselves and set their own industry standards and benchmarks as to proper conduct towards tenants.

I have seen countless examples of abuse of market power by shopping centre landlords and seen the devastating effect this has on the lives of retailers, their families and their staff. Much unconscionable conduct is kept from the public eye, protected by confidentiality clauses.

- 1.3 I have reviewed hundreds of Retail Leases and been involved in numerous Retail Lease disputes, mediations and settlements. In my view the *Retail Leases Act 1994* and the procedure for mediation before the Retail Tenancy Unit makes a significant contribution to resolving Retail Lease disputes. I commend the 2005 and 2006 amendments to the *Retail Leases Act* and believe that overall this Act does provide a very good platform for the resolution of retail shop disputes, both from a landlord and a tenant perspective. The requirement of the parties to attempt mediation is a very positive and beneficial requirement. It enables the party with less financial resources to have a venue for dispute resolution, without the need to incur the significant and sometimes prohibitive cost of litigation. Further it enables the parties to restore and to build on, their relationship as landlord and tenant. I understand that 81% of retail lease disputes are resolved either at mediation or shortly after mediation. The provisions of the Act which deal with misleading and deceptive conduct, unconscionable conduct and pre-lease misrepresentation allow an aggrieved tenant to seek recourse to have grievances addressed firstly by mediation and, if necessary, proceedings in the Administrative Decisions Tribunal. In my view, the legal framework is working ( whilst it can be improved), possibly the biggest barrier is communication of rights to tenants. The Retail Tenancy Unit is

doing great work in the process of educating tenants of their rights and obligations. I note that sometimes tenants fear that in seeking legal remedy for their issues against the landlord, that the landlord could retaliate against such tenants by refusing to give them good locations, whether in that particular centre or in other shopping centres owned by that landlord. This concern is harder to address.

**2 Possible suggestions as to what can be done to overcome market power of large shopping centre landlord in the manner in which they deal with tenants**

The problem overall, in my view, is not a legal one. The relevant State legislation is addressing these issues. The problem is the imbalance of market power of the shopping centre landlord.

I appreciate that some of the ideas set out below are not fully formed, they may be the basis of a workable idea that could assist the problems experienced by shopping centre tenants. I make some suggestions for consideration by the Commission including some amendments to existing retail lease legislation:

- (a) The Retail Lease Legislation should prohibit the passing on of certain expenses to the tenant:
- The landlord should be prohibited from passing on the cost of the survey of the store. This is a requirement of one of the major shopping centre owners.
  - The landlord often requires the tenant to pay for the landlord's architects to review the shop design. This expense should not be passed on to the tenant.
  - Landlord can make unreasonable demands on tenants in relation to fit out and refurbishment obligations – all at the tenant's costs and frequently these demands are unreasonable. As an example, one of Sydney's major retail shopping centre landlord required a tenant who had been in the one location for 25 years and who refurbished their shop 5 years ago, to move to a new location as the landlord would not renew the lease at this location and the Disclosure Statement specifically required the tenant to provide "all brand new fixtures and fittings.". We replied to the solicitors for the landlord stating that this view was environmentally irresponsible. Whilst the solicitors for the landlord said that its client sees itself as a good corporate citizen, the request was rejected.
  - In addition, the lease can require the tenant to only use approved contractors and in relation to shop hoardings, sometimes it is only the centre's contractor that may be used. This conduct is uncompetitive.
- (b) The Retail Lease legislation should prohibit the landlord from forcing the tenant to disclose its sales to the landlord. The problem with this information is that the landlord can use this information to increase the rent of the tenant just to point before the tenant cannot say no to a rental increase and secondly, the consequence of which is even worse, if the landlord knows that a certain business is doing well, the landlord then approaches a

competitor in the similar business, rather than showing loyalty to the existing tenant, the landlord can use this information to damage the business of the tenant.

2. Maybe shopping centres should be strata titled so that then there will be a competitive market as there would not be the single landlord, but many landlords. That way there would be a competitive market for space within the shopping centre. If a tenant was negotiating a lease and considered the owners asking rent to be too high, that tenant could approach another strata owner in the centre with a view to lease their premises. Also, it would allow tenants the opportunity to be owner occupiers. This would overcome to some extent the monopolistic power of a single landlord.
3. There should be an Ombudsman or a representative who would listen to Retail Lease disputes where a landlord has abused its market power. An aggrieved tenant is not always right - there are cases where a tenant's lack of performance is due to its own conduct and has nothing to do with the landlord. If there was an Ombudsman or person who was impartial but could address some concerns, I think this could create a mechanism to control the excesses of abuse of market power by shopping centre landlords.
4. Maybe the landlord should not be able to charge a fixed rent in a shopping centre in all circumstances. Maybe rent needs to be linked to turnover or linked to traffic counts in a shopping centre. There are many cases where the tenant signs a lease but then the shopping centre fails to deliver the expectation and the tenant is without recourse but the landlord is still entitled to the rent as set out in the lease and entitled to enforce payment of rent and if necessary terminate the lease and sue the tenant for the damages. The traditional lease document in my view allows considerable protection for the landlord and little protection for the tenant. I often think that there must be a new legal relationship and appropriate legal agreement to replace the traditional lease which tries to alleviate the market imbalance. In particular I submit that the rent should not be fixed. The rent should somehow tie into the performance of the centre. This would address the issue of market abuse to some extent. I appreciate that this idea is not fully developed but I raise my thoughts for the Commission to consideration.
5. Maybe there should be a prohibition of one landlord owning a number of shopping centres in a concentrated area where the effect is to substantially lessen competition.

If I can be of any further assistance to the Commission please do not hesitate to contact me.

Yours sincerely

**HERRO SOLICITORS**

**Anthony Herro**  
**Principal Solicitor**

27<sup>th</sup> July 2007