



Real Estate Institute of Australia

**REIA SUBMISSION TO THE PRODUCTIVITY COMMISSION PUBLIC HEARING
ON THE MARKET FOR RETAIL TENANCY LEASES IN AUSTRALIA**

BACKGROUND

1. On 19 July 2007, the Commonwealth Treasurer, the Hon. Peter Costello MP, requested that the Productivity Commission (PC) undertake an *Inquiry into the Market for Retail Tenancy Leases in Australia*, including its structure, function, competitiveness and regulation. The PC subsequently published an issues paper followed by the release of a draft report in November 2007.
2. The Real Estate Institute of Australia (REIA) is the peak national professional association for the real estate industry in Australia. The REIA has eight members, comprised of the State and Territory Real Estate Institutes, through which about 80% of real estate agencies are collectively represented.
3. The REIA met with PC representatives on 11 July 2007, to discuss the nature of the Inquiry and to provide a preliminary industry viewpoint. An REIA submission was tendered in respect of the issues paper.

PURPOSE

4. This document constitutes a preliminary REIA response to the draft report on the *Inquiry into the Market for Retail Tenancy Leases in Australia*, and is provided for the consideration of the PC prior to the public hearing to be held 1 February 2007 in Canberra, at which the REIA will be represented.

ISSUES

Overall Impression of Draft Report

5. Overall, the REIA is pleased with the PC's draft report on *The Market for Retail Tenancy Leases in Australia*. The draft report has comprehensively addressed the terms of reference as handed down by the Commonwealth Government and contains an array of useful findings and recommendations which aim to improve the retail tenancy market.
6. While highlighting the merits of improved information availability and transparency in the marketplace, the PC report has, in itself, consolidated a wealth of contemporary information concerning the retail tenancy market for the benefit of tenants, landlords, property professionals and policy makers.

7. The REIA considers that the current draft largely reflects the REIA's previously espoused view that the market is generally competitive and devoid of fundamental flaws that systematically disadvantage landlords or tenants. The REIA agrees that the retail tenancy market is functioning reasonably well, although it has been burdened by overly-prescriptive regulation by the various State and Territory Governments. Although well intentioned and aimed at resolving perceived imbalances between the negotiating power of landlords and tenants, independent regulation creep has led to the development of numerous inconsistencies between the various jurisdictions, which when viewed from a national perspective, are likely to be constraining the efficiency of the retail tenancy market. Lower efficiency results in higher costs for landlords, tenants and ultimately consumers.

8. Indeed, as suggested within the overview of the report, retail tenancy regulation has now arguably tilted in favour of some tenants. As such it often disadvantages businesses seeking lease terms outside of those prescribed, can enable some tenants to avoid contractual obligations and can result in some premises remaining vacant due to risks involved in short-term tenanting.

9. The rapid accumulation of more and more prescriptive retail tenancy legislation (including the availability of market information and low-cost dispute resolution services) appears to have done little to alter the perception of many small retailers that they are at a disadvantage when negotiating retail leasing terms with their landlord. The REIA suggests that this perception is unfortunately inherent within the landlord-tenant relationship. While tenants should (and do) have certain rights to the unimpeded enjoyment of premises as per the tenancy agreement, no amount of regulation will alter the fact that the landlord is the owner of the premises (enjoying the normal rights of ownership under common law) and the tenant is a temporary occupant. To try and regulate otherwise simply adds unnecessary administrative and compliance costs.

10. There is a balance to be achieved between the needs and motivation of both landlord and tenant. Like their retail tenants, landlords are seeking to maximise the return on their own business investment, which is the business premises. Tenants should not assume a right to occupy premises indefinitely, particularly if they are not prepared to pay a competitive market rent. If market rents were not able to be sought, premises would not be put to their best use, lowering productivity in the retail sector.

11. There is however much tenants can do to maximise their own bargaining position including; taking a rational and balanced perspective, accessing up-to-date market information, engaging the services of property professionals (real estate agents and valuers), obtaining legal advice, and obtaining financial advice.

12. As determined by the PC, when things do go wrong, there are a range of readily accessible and moderately priced dispute resolution services available in all Australian jurisdictions. There are also financial counselling services available.

13. The REIA generally agrees with the main findings of the PC that the primary mechanisms available for improving the retail tenancy market are:

- a. improving, where practicable and cost effective; education, information and dispute resolution processes; and
- b. removing the more restrictive elements of retail tenancy legislation, and divisions between jurisdictions and with the broader market for commercial tenancies.

14. The proposed principles for assessing regulation in retail tenancies as contained in Box 1 of the draft report appear reasonable and the REIA agrees that State and Territory Governments should immediately desist from further increasing the prescriptiveness of retail tenancy regulation or introduce further inter-jurisdictional inconsistencies.

15. The REIA's responses to the specific recommendations and further information requests contained in the draft report are presented below.

PRODUCTIVITY COMMISSION RECOMMENDATIONS

Recommendation 1

The following measures should be pursued by State and Territory governments to further improve transparency and accessibility in the retail tenancy market.

- *Enhance the use of simple language in all tenancy documentation and provide clear and obvious contact points for information on leases and dispute resolution.*
- *Elaborate the significance of jurisdictional differences in the definition of unconscionable conduct and align definitions where practicable.*

16. **Simple Language.** The REIA generally supports improving the transparency of the retail tenancy market and improving accessibility of dispute resolution systems. While it is preferable for simple language to be used in leasing documentation, it must be remembered that the lease language must also conform with that used within the legal profession. Ultimately the lease is a binding contract between the landlord and the tenant and must be enforceable under the law.

17. The REIA suggests that the most appropriate place for simple language (or indeed 'plain English' – see Recommendation 2) would be within pre-contractual disclosure documents as used in the most jurisdictions including the ACT. In the ACT, the disclosure document sets out the major terms and conditions of the contract including rents to be paid in a simple, plain English, format. While the disclosure statement is not in itself a lease, regulation in the ACT permits leases to be made null and void if they deviate from the disclosure statement.

18. While this would not remove the onus on the potential tenant to obtain legal advice prior to signing the lease, this would prove a practical alternative to governments involving themselves in prescribing lease language, which is what it is for legal reasons.

19. **Clear and Obvious Contact Points.** The REIA understands that most lease contracts provide a clear and obvious contact point in the event that the tenant wishes to make a complaint concerning the lease terms and conditions. This contact point is usually the landlord or managing agent, who is generally the best point of contact in the first instance as there is a good chance that minor disputes can be resolved without the involvement of third parties.

20. Although the perception that there are frequent disputes concerning retail tenancy leases appears widespread, the evidence contained in the PC's draft report indicates otherwise, with just 3,300 (around 1%) complaints received annually in a total market of 290,000. Given the significant churn rate of 58,000 new leases being written each year, this is an extraordinarily low complaint rate. The REIA agrees with the PC that, with around 80% of these complaints being resolved via mediation, the current dispute resolution systems operating across the various jurisdictions are easily accessible and working reasonably well.

21. The inclusion of clear and obvious contact points for dispute resolution within lease documents has obvious benefits for all parties to the lease agreement. While supporting such an inclusion, the manner in which this is achieved should not be prescribed. Instead, the REIA suggests that an approach be taken similar to that proposed by the REIA at Recommendation 2, below.

22. **Unconscionable Conduct.** While supportive of the alignment of unconscionable conduct provisions, this issue is primarily a matter for State and Territory Governments and their enforcement agencies. The very notion of unconscionable conduct can be ambiguous and the imposition of a single national, easy to comprehend definition would be of benefit to the business community more generally. There is no reason, in principle, why different jurisdictions should apply differing definitions of this concept.

23. As a starting point, the definition of unconscionable conduct used by the ACCC should be contrasted against those used in the various State and Territory jurisdictions, with a view to arriving at a single standard definition. Once a standard definition has been determined, the definition should not be altered without the agreement of all jurisdictions. Given the generic nature of the concept, it is likely that any uniform definition would be enduring.

Recommendation 2

State and Territory governments should seek to improve the consistency of lease information across jurisdictions in order to lower compliance and administration costs. They should:

- *Encourage nationally consistent (plain English) models for retail tenancy leases and for tenant and landlord disclosure statements (for example, all jurisdiction and other specific provisions could be set out in annexes to the standard documents).*
- *Institute nationally consistent reporting by administering authorities on the incidence of tenancy inquiries, complaints and dispute resolution.*

24. **Improving Consistency of Lease Information.** While national consistency is laudable, this should not be so prescriptive that some flexibility is removed. Standard retail lease documents were once in use in jurisdictions such as NSW, however these fell out of favour due to their inability to stay abreast of a rapidly changing leasing market. The REIA does not support the implementation of an entire national standardised lease agreement or disclosure statement, which would be likely to constrain market flexibility.
25. The REIA proposes that a more practical alternative model would be for governments to simply prescribe the elements that must be contained in any lease agreement or disclosure statement and then leave it to the market place to prepare the best lease document for any given situation. The REIA considers that it is not the purview of governments to be prescribing actual lease documents in a healthy, competitive market. This should be influenced in part by factors of supply, demand and legislative interpretation.
26. Once installed, it would be difficult and time consuming for industry to modify the standard lease document in response to a changing market. Any move to do so may even arouse suspicions by protective governments or retail representatives that any proposed changes benefiting landlords must be against the interests of tenants. Governments are also likely to seek to unilaterally modify the standard lease document over time in response to 'perceived' problems or single high profile events that have gained media attention. It is entirely possible that tenants may even be discouraged from seeking their own legal advice if they were to rely on standardised documents (as this may then be seen as an unnecessary cost).
27. The REIA's proposed alternative would allow flexibility in the marketplace while also ensuring that all lease agreements and disclosure statements contained the necessary prescribed content. This proposal does not require an ongoing administrative role for governments in the design and maintenance of standard lease agreements, and is consistent with the PC's calls for less prescriptive legislation.
28. **Nationally Consistent Reporting:** The REIA supports nationally consistent reporting by administering authorities on the incidence of tenancy enquiries, complaints and dispute resolution. This however may be difficult in the absence of nationally consistent leasing legislation, given that breaches in one jurisdiction may not necessarily amount to breaches in another (e.g. on the basis of differencing definitions of unconscionable conduct).
29. If national reporting is to occur, consolidated results should be made available publicly for the benefit of landlords, tenants and policy makers within the constraints of the Privacy Act. There are also many questions that must be addressed before national reporting could occur such as:
- a. defining the standards upon which to report (e.g. contextualising enquiries);
 - b. determining limitations on data use and comparison;
 - c. determining an agency responsible for the collection of data on a national basis;
 - d. determining a mechanism to interpret and incorporate data on the nature and outcomes of dispute which proceed to the courts; and
 - e. determining a funding and governance model for the national collation of the results.

Recommendation 3

State and Territory governments should relax key restrictions in retail tenancy legislation to better align the regulation of the retail tenancy market with the broader market for commercial tenancies.

30. **Relaxation of Key Restrictions.** The removal of unnecessary restrictions in retail tenancy legislation is likely to result in savings for both businesses and governments. Unnecessary regulation leads to unnecessary costs, which in turn leads to more expensive tenancies and consumer prices.

31. The REIA agrees that a specific review should be implemented by governments to examine the potential to remove key restrictions across all jurisdictions in areas including minimum (or maximum) lease terms, preferential rights of lease renewal, assignment and sub-letting, rent reviews, limits on rent inclusions, and recoverable outgoings. The PC's proposed 2 – 5 year time frame is a realistic period in which to conduct such a review. One option that could be explored should be a system similar to that in the ACT wherein there is some differentiation in the entities covered by the prescriptive elements of the retail tenancy regulations. In the ACT, all entities are presumed to be covered except for public companies and those seeking tenancies with a floor area in excess of 1,000m². The basis for this differentiation is that larger or more professional entities do not require the same level of protection and commonly regard any prescribed protections as an unnecessary restriction on their right to negotiate their own leasing terms and conditions.

32. The removal of many of these key restrictions will also support the REIA's proposal under Recommendation 2 for governments to move away from prescribing actual lease documentation and disclosure statements in favour of prescribing broader, more generic, elements that must be included. Basic, universal requirements are likely to be more successful when also underpinned by enhanced information availability and dispute resolution services.

33. **Aligning of Retail and Commercial Tenancy Legislation:** The REIA considers that there are both fundamental similarities and differences between the retail tenancy market and the broader commercial tenancy market. While in both cases space is let to a tenant for the purposes of operating a business, retail tenants tend to be more dependent on a stable location for their market presence and may be subject to additional obligations such as maintaining specific opening hours, carrying out regular fitouts or contributing to a promotional fund. Retail tenants may also be subject to being relocated within a larger complex at the behest of the landlord if that is considered the best course of action for the overall tenancy mix.

34. For these reasons, the REIA asserts that it will not be possible to completely align retail and commercial tenancy legislation. At the very least, the retail tenancy market must be considered to be a sub-set of the broader commercial tenancy market, and some differentiation will be required.

35. In terms of the principles underpinning the leasing of retail or commercial space however, it should be possible to improve the current regulatory alignment between the two sectors. The REIA would support an examination of the potential for closer alignment in each jurisdiction to be carried out as part of the process of arriving at nationally consistent retail tenancy regulation (see Recommendation 4, below).

Recommendation 4

As unnecessarily prescriptive elements of retail tenancy legislation are removed, State and Territory governments should seek, where practicable, to establish nationally consistent template legislation for retail and commercial tenancies available to be drawn down to each jurisdiction.

36. As previously espoused, the REIA supports the development of nationally consistent legislation governing both retail and commercial tenancies. Greater consistency in this regulatory area will lead to greater efficiency in the marketplace, in turn leading to direct savings for landlords, tenants, governments and consumers. There are no boundaries on the Australian business map and larger landlords, tenants and even many consumers operate across multiple jurisdictions.

37. The REIA argues that the removal of unnecessarily prescriptive elements and the drawing up of nationally consistent template legislation are inextricably linked and must be carried out concurrently. It will not be possible to implement a harmonised regulatory system while ever State and Territory Governments are not able to agree on those elements which are overly prescriptive and while State and Territory Governments have not agreed 'in-principle' to do so. From a business efficiency perspective, it is also preferable to avoid multiple rounds of regulatory change that would require businesses to constantly change procedures throughout the review process.

38. The REIA suggests that ideally, State and Territory Governments should first agree in principle to move towards nationally consistent template legislation. Governments should then instigate a review aimed at identifying unnecessarily prescriptive elements of current legislation, with a view to removing these as part of moving to a national template. Once the national template has been agreed, it should be implemented across all jurisdictions (more or less) simultaneously, to supersede current legislation and thereby also remove the overly prescriptive elements.

39. Governments must then be bound not to modify the legislation without the agreement of the majority of jurisdictions. If a decision is taken to change the legislation then all jurisdictions must follow suit. A regular review process should be implemented such that jurisdictions have an opportunity to raise particular issues and so that industry has an opportunity to feed into the maintenance of appropriate legislation. State and Territory Governments should implement a harmonised education program to inform the retail sector of any regulatory changes that have been made.

Recommendation 5

While recognising the merits of planning and zoning controls in preserving public amenity, States and Territories should examine the potential to relax those controls that limit competition and restrict retail spaces and its utilisation.

40. The REIA supports examining the potential to relax controls that limit competition and restrict retail space and its utilisation.

41. Planning and zoning controls play an important role in the development and shaping of our cities. While these controls aim to manage the competing interests of various community members and maximise the utility and amenity of both public and private space, there are often unintended consequences which reduce the efficiency of important sectors of the community economy.

42. Planning and zoning controls not only influence the permitted use of land and buildings, but also the value of those areas. When the supply of land for retail development is limited, the price will rise accordingly. Overly restrictive controls can prevent economic development in the retail sector (and other sectors such as housing and industrial), by either prohibiting certain types of development, or making it so costly or uncertain that required development does not occur.

43. Given their often localised application, it is somewhat difficult to generalise the impact of planning and zoning controls on the retail sector. In places such as Wagga Wagga, NSW, there is a broad commercial zone characterised by a retail 'high street' with malls opening onto the strip. New malls may be built along the strip and the availability of retail space could be said to be primarily limited by economics more so than the planning restrictions. In other areas such as Canberra, each block is purpose zoned creating a situation wherein every major new development is subject to a complex approval process that potentially requires rezoning of the block. Competition for available retail space is more tightly regulated in these situations. While a new mall may open next to an existing mall in Wagga Wagga, these opportunities are severely limited in many areas of Canberra.

44. While consumers generally appear to have a preference for shopping in one central location (as demonstrated by clustering of restaurants, car dealerships and other similar retailers), there are pros and cons of regulating development in this way. If retail space was limited to a single, under-sized mall in a given location, the lack of available retail space will cause rents to increase. If however, there are too many of these developments in close proximity, they may all suffer due to an overall lack of consumer traffic. So, while supportive of reviewing the potential to relax planning controls in some areas, the REIA would not support the complete abolition of planning and zoning restrictions.

FURTHER INFORMATION REQUESTS

Lease Registration

The Commission invites comments on the feasibility and benefits of more widespread lease registration and facilitation of this process by landlords.

45. As determined by the PC, lease registration is currently available in all States and Territories and there is little information available concerning whether or not the registration of leases has led to an improved balance of (perceived) bargaining power between landlords and tenants. It appears however that the registration processes vary by jurisdiction and that the information collected via this process is not always made available to the public.

46. Lease registration in itself represents an administrative overhead that could easily be avoided. However, on the other hand, lease registration is a means by which governments can collect revenue, reference lease agreements for enforcement purposes and collect information concerning the retail leasing market.

47. If leasing registration is to become more widespread, certain questions should be addressed to ensure that the benefits of doing so outweigh the administrative cost of registration. For instance:

- a. what is to be achieved via lease registration?;
- b. what is the threshold for lease registration? (i.e. the term or value of the lease);
- c. what information is to be collected and made public? (i.e. key details, the entire lease document, subsequent market rent reviews);
- d. who should be responsible for lease registration? (i.e. the landlord or tenant);
- e. who will be able to access registered lease details?; and
- f. other issues such as the privacy concerns of the parties to the lease.

48. The REIA suggests that a leasing register would need to contain entire lease agreements if it was to provide useful information to the market. It is often the terms, conditions and incentives contained in a lease agreement that will be of interest to the market and the rents charged are entirely dependent on these factors. However, the potential publication of entire lease agreements raises issues concerning the privacy of parties to the lease and the level of government resources required to maintain a workable registration and access system.

49. It should be remembered that potential tenants may already utilise the services of property professionals, such as agents or valuers, if they are seeking an opinion concerning current market rents.

50. Due to the complexities surrounding this issue, this proposal should be reviewed in more detail prior to the PC making any recommendation concerning the registration of lease agreements.

Voluntary Code of Conduct

The Commission invites evidence on the feasibility and benefits associated with the introduction of a voluntary national code of conduct for shopping centre leases enforceable by the ACCC.

51. The introduction of a voluntary code of conduct for shopping centre leases is a matter for the retail shopping centre sector. The REIA simply suggests that any code of conduct would need to be developed in consultation with both landlords and tenants and be binding across the entire industry. A code should not be costly to industry and should not impose more compliance requirements.

52. It maybe problematic and difficult to achieve a truly workable code of conduct that is supported by both the landlord and the tenant.

Nationally Consistent Framework

The Commission invites comments on the desirability and feasibility of establishing a nationally consistent framework for tenancy leases through the drawing down of nationally consistent template legislation for commercial (including retail) leases to each jurisdiction.

53. The REIA supports the implementation of nationally consistent retail and commercial legislation as outlined at Recommendation 4, above. However, the REIA does not support the extension of this legislation into areas such as the prescription of standard lease contracts or disclosure statements.

54. The feasibility of establishing nationally consistent tenancy legislation will depend largely on the ‘in-principle’ agreement of all States and Territories and the implementation of a workable process for reviewing current legislation and the drafting of a model leasing act. The REIA suggests that the best method for achieving national consistency would be for States and Territories to review the current legislation (with a view to removing overly prescriptive elements), agree upon the elements that must (or must not) be included in all lease agreements, draft legislation that reflects these requirements and mandate that a pre-contractual disclosure statement (in plain English) outlining these elements be provided to potential tenants.

Costs and Benefits

The Commission invites evidence on the costs and benefits of its draft recommendations for retail tenants, landlords, investors and the community generally.

55. The REIA is not in a position to fully assess the costs and benefits of the PC’s draft recommendations, other than to say:

- a. removing unnecessarily prescriptive elements will benefit both landlords and tenants;
- b. businesses, retailers and consumers operating across various jurisdictions are likely to be the largest beneficiaries;
- c. governments may face initial costs associated with legislative change but these will be more than off-set in the longer term by simplifying and harmonising retail tenancy administration;
- d. harmonising concepts such as unconscionable conduct will have benefits in the broader business community; and
- e. harmonised and simplified legislation will have additional intangible benefits such as increasing business confidence when dealing with tenancy issues.

SUMMARY

56. The REIA largely supports the recommendations contained in the PC's draft report on the *Inquiry into the Market for Retail Tenancy Leases in Australia*. The current draft largely reflects the REIA's previously espoused view that the market is generally competitive and devoid of fundamental flaws that systematically disadvantage landlords or tenants.

57. The REIA generally agrees with the main findings of the PC that the primary mechanisms available for improving the retail tenancy market are:

- a. improving, where practicable and cost effective, education, information and dispute resolution processes; and
- b. removing the more restrictive elements of retail tenancy legislation, and divisions between jurisdictions and with the broader market for commercial tenancies.

58. Specifically, the REIA supports:

- a. encouraging the use of simplified language, provided that due regard is paid to the requirement for appropriate legal language required in contracts;
- b. the inclusion of clear and obvious contact points for information or dispute resolution within disclosure statements. The landlord, or their representative, should remain the primary contact point within the lease document;
- c. a uniform national definition of unconscionable conduct;
- d. improving the consistency of lease information, by prescribing the elements that should be contained within lease documents;
- e. nationally consistent reporting by administering authorities on the incidence of tenancy enquiries, complaints and dispute resolution, provided that the results are also made public for the benefit of the retail sector;
- f. the relaxation of key restrictions such as those relating to minimum (or maximum) lease terms, preferential rights of lease renewal, assignment and sub-letting, rent reviews, limits on rent inclusions, and recoverable outgoings; and
- g. the establishment of nationally consistent template legislation for retail and commercial tenancies.

59. The REIA does not however agree with the PC's proposals that may lead to completely standardised leasing documentation or the complete removal of all regulatory differentiation between commercial and retail leasing markets. The REIA proposes that a more practical alternative model would be for governments to simply prescribe the elements that must be contained in any lease agreement or disclosure statement and then leave it to the market place to prepare the best lease document for any given situation. The REIA considers that it is not the pervue of governments to be prescribing actual lease documents in a healthy, competitive market.

60. The REIA supports a further review of the potential for more widespread lease registration and the potential to relax those planning and zoning controls that limit competition and restrict retail spaces and its utilisation.

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