

University of Reading

**An Evaluation of the Policy Implications for
the UK of the Approach to Small Business
Tenant Legislation in Australia**

Volume 1 – Main Report

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Executive Summary

Aims, objectives and methods

The aim of the research was to examine perceptions of the effectiveness of small business tenant legislation in Australia and to provide a preliminary evaluation of its potential use in the UK.

The objectives were to:

- Identify the policy aims and objectives of small business tenant legislation.
- Determine the nature and scope of small business tenant legislation in the Australian States in terms of the identification and classification of small business tenants and premises and examine the different strands to the legislation and how they are perceived to impact on the landlord and small business tenant relationship.
- Identify the perceptions of stakeholders in the Australian leasing market and evaluate the perceived effectiveness of the legislation in the context of the policy aims and objectives.
- Discuss the possibility of similar legislation being applied to the UK and provide a preliminary conclusion on the advantages and disadvantages with this option.

The objectives have been addressed by a combination of literature review, analysis of lease terms and an interview survey carried out mainly within a specific case study area, the State of Victoria.

Summary of findings

There is no national uniform tenancy code in Australia. Responsibility for legislating on commercial landlord and tenant issues lies at State or Territory level, despite numerous calls from Government Committee reports, and landlords' and tenants' organisations for national laws.

Since the 1980s, all States in Australia have developed legislation or mandatory codes to protect small business tenants against the abuse of market power by landlords, particularly large shopping centre landlords.

Voluntary codes of practice have been dismissed as ineffective and now all States have legislation or mandatory codes. In New South Wales the voluntary code was ignored despite being backed by both landlords' and tenants' organisations.

The legislation is primarily aimed at retail tenants although the scope of the legislation varies between the States; in Victoria retail is defined quite widely as retail services which includes some office users.

Attempting to isolate part of the market for legislation has caused major issues for all States and definitions of retail premises vary from a very blunt floorspace threshold to more complex arrangements of rent, and some States also exclude listed companies from the legislation. The result is that many small commercial users are excluded from the protection of the Act while some large nationally operated companies are included. The situation is unsatisfactory and no legislation uses number of employees to define a small retail tenant.

The legislation is often administered by lease registrars or commissioners and they have responsibility for education, investigation of non-compliance under the legislation and dispute resolution. In Victoria, 70% of the work of the Small Business Commissioner relates to retail tenancy issues.

The information available to small retail tenants is usually comprehensive and the legislation requires landlords to give out information brochures and a copy of the draft lease to any prospective tenant upon the opening of negotiations. This is in stark contrast with the UK. Penalties include fines and termination rights if leases are entered into without the provision of information at the appropriate time. Property professionals in Australia are convinced that the awareness of business tenants is increased by the information provision as it forces tenants to consider the implications of leases more closely, or drives them to seek earlier professional advice.

Some days before the lease is signed, the landlord must lodge a disclosure statement with the tenant and this statement includes most issues including expected costs during the lease and expected events, such as planned alterations to the shopping centre, which must be disclosed. Again non-compliance can lead to a legitimate withholding of rent or termination of the lease and/or fines. In some States tenants are also required to disclose and this can include the provision of business plans.

Legislation usually prescribes a minimum lease term of 5 years, bans upwards-only reviews and prescribes many other terms of the lease. Since the ban on upwards only has been implemented, market reviews have largely disappeared and fixed increases or increases based on consumer price indexes are common.

The right to renew is not granted by any State legislation, the closest is in Australian Capital Territory and South Australia where a preferential right to renew the lease exists. This has been described as the most contentious issue in the Australian landlord and tenant debate and seems set to continue. The landlord's case for the right to manage the centre seems to hold sway at present over the tenant's claims of misuse of power at lease expiry.

The dispute resolution process in many States is based on compulsory mediation prior to any case being allowed to proceed to court. In Victoria, the Small Business Commissioner administers the system and has a 75% settlement rate of cases prior to or at formal mediation sessions. They are committed to low-cost, quick dispute resolution and the system came in for virtually universal praise.

There are fair trading laws in Australia which have been incorporated into virtually all retail lease legislation. Landlords appear nervous of the unconscionable conduct provisions and the implications for any adverse publicity of being found to have acted

unconscionably in negotiations. Despite the difficulties in bringing a successful action, landlords would rather be found guilty of non-compliance of a provision in the Act than unconscionable conduct.

Policy implications for the UK

If the UK government were to consider partial legislation for small business tenants, nothing in the policy and application of the Australian legislation would change the current emphasis from all small business tenants to retail tenants only.

The study of Australia also identifies the difficulties of implementing legislation across part of the market; defining the scope of the Act has caused numerous difficulties over the past 20 years and there is nothing to think that it would be any easier to implement in the UK if partial legislation were considered.

The information and disclosure provisions are perceived to have improved the awareness of small business tenants; at very least it has persuaded them to take professional advice early. It would appear that mandatory information could be the key to achieving UK Government objectives concerning the awareness of small business tenants. It could be made mandatory for landlords and their agents to provide all prospective tenants with a copy of the Code and the proposed lease, with fines and termination rights for non compliance. Disclosure statements also have a role to play in increasing the ability of small business tenants to get a fair lease.

Overall, it is plain that some of the themes of lease legislation in Australia address the same issues of small tenant awareness that exist in the UK. The most obvious ones are the information and disclosure provisions and the use of lease registrars or commissioners to administer education, compliance and dispute resolution. Given the failure of the property industry in the UK to voluntarily ensure proper dissemination of the two Lease Codes, the success of mandatory information provisions and easier dispute resolution processes could be considered in the UK to solve the small business tenant policy issue.

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Chapter 1 - Background to the Research

At the end of the 1980s, the UK commercial and industrial property market entered the longest bear market since the end of the Second World War. There had been one other serious recession in the early 1970s but rents recovered to previous levels within a normal rent revision period, which had just fallen to around 5 to 7 years. Both landlords and tenants respectively received and paid higher rents at the next rent review.

However, despite having escaped falls in rent, institutional landlords protected themselves from future recessions by introducing the ratcheted upwards only rent revision clause into leases (normally every 5 years) and by 1990 this had become a standard clause, along with 20-25 year terms, few break options and tenant responsibility for all repairs and insurances. Crosby *et al* (2000) record that in 1990 around 90% of commercial leases by value within the Investment Property Databank (IPD) (comprising property held by the major landlords; both financial institutions and property companies) were let on this sort of lease which became known as the “institutional” lease in the UK.

In 1990 rents fell by significant amounts. Figure 1.1 indicates that the all property estimated rental value index of IPD rose by 10% in 1986, 19% in 1987, 23% in 1988 and 15% in 1989. Unfortunately it fell by 9% in 1991, 12% in 1992 and 8% in 1993. It fell again by 1% in 1994 before a stuttering recovery began in 1995 and 1996. It was only in 1997 and 1998 that rental values grew significantly (IPD, 2005). There is evidence that the information on which the IPD figures are based is distorted in this recessionary period by the use of letting incentives and some of the reported figures are based on headline rather than effective rents. The reductions in rental value can be viewed as minimums and the true extent of the falls in rental value are thought to be greater (Crosby and Murdoch, 2001).

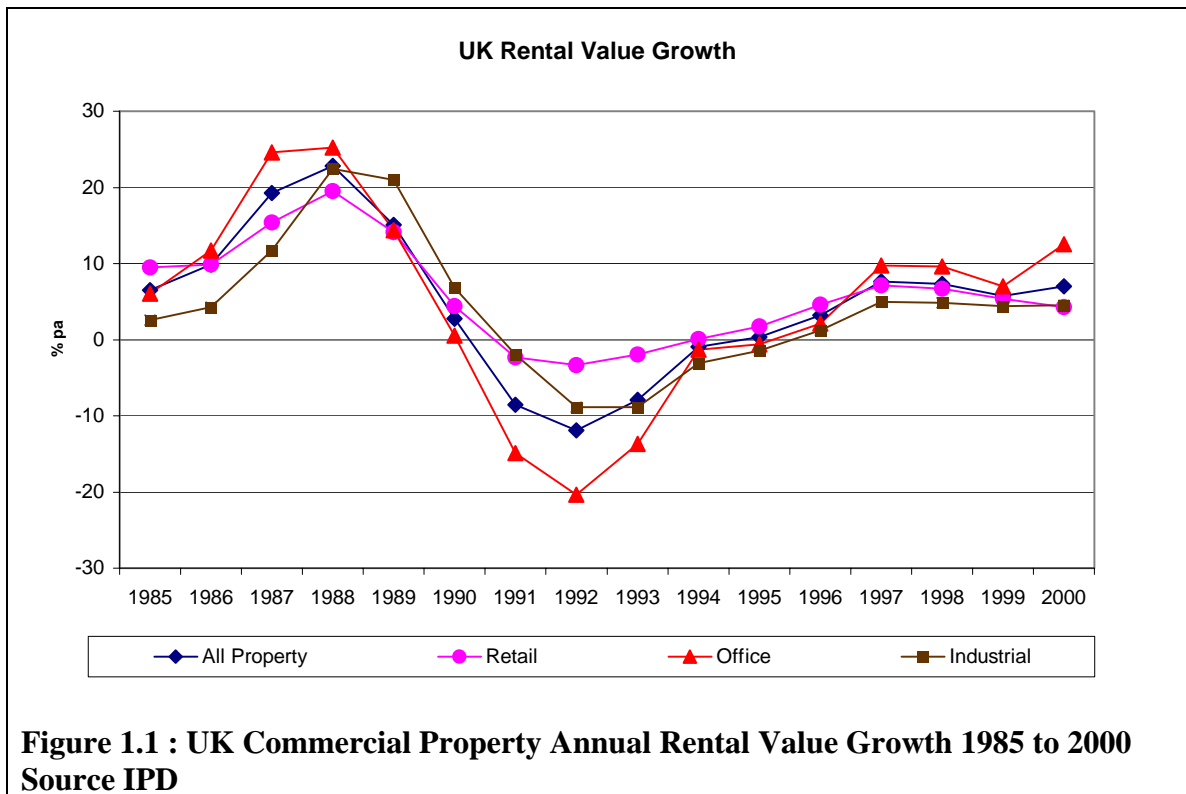


Figure 1.1 : UK Commercial Property Annual Rental Value Growth 1985 to 2000
Source IPD

Due to the economic recession in the early 1990s, tenants were faced with falls in the earning potential of their businesses, hence the fall in property market rental values flowing through from the business downturn. They hoped to get reductions in rent at the rent review to compensate but the ratchet clause came into operation to maintain previous levels.

Tenants responded by allegedly filling the Government postbag with complaints about their inability to occupy at market rents and the unfairness of landlords being protected from the effects of economic recession. Given that many of them commenced occupation during the building and letting boom of the late 1980s and would have occupied under institutional leases, tenants were faced with the prospect of paying late 1980 rental levels for a long term into the future.

Using an Adam Smith Institute report (Burton, 1992) into retail rents as evidence, the UK Government published a consultation paper in 1993 and suggested that it was minded to intervene in the market. It isolated the three main issues of the Burton Report, upwards only rent reviews, confidentiality agreements (where landlords attempted to restrict the free flow of market information about rent agreements) and dispute resolution, as its three principal targets.

Property industry responses to the consultation convinced Government to try a voluntary Code of Practice launched in 1995 (RICS, 1995). The operation and effectiveness of the Code was monitored by the University of Reading (Crosby *et al*, 2000) and they suggested that the Code was not working. However, they also found that some of the changes the Government wanted had taken place because of the changing balance of market power between landlord and tenant. This was because of the poor state of the lettings market in the early 1990s.

A revised Code of Practice, still voluntary, was launched in 2002 (RICS, 2002) and the University of Reading again was asked by Government to monitor it (Crosby *et al*, 2005). In the same year the Government issued a policy statement which followed the recommendations of the report. It moved assignment and subletting provisions to the top of its agenda while still keeping upwards only rent reviews on the agenda.

In Crosby *et al* (2000), the University of Reading monitoring report had identified the lack of awareness of small business tenants concerning leasing issues as an area of concern and they reiterated these concerns in their second monitoring report (Crosby *et al*, 2005). So in the UK Government statement of 2005, it identified the awareness of small business tenants as its third major concern.

To summarise, throughout the extended period since 1992 when the Government first put commercial lease reform onto its policy agenda, they have not taken the legislative option, preferring to persuade the parties to pursue voluntary reform through the mechanism of voluntary codes of practice. During 2006, a working group has been devising a third voluntary code and the Government has pledged to continue to monitor the situation after that is published.

This research concentrates on the third policy issue, the awareness of small business tenants. The Crosby *et al* (2005) findings were that there are differences between leases taken by small businesses and those taken by medium and larger sized companies. Differences in lease length are indicated in Tables 1.1 and 1.2

Table 1.1 : Average Lease Length – IPD Unweighted - to lease expiry or first break

	Large	Medium	Small	Micro	Unknown
Retail	11.3	9.8	6.4	6.5	4.3
Office	6.3	5.0	4.5	4.4	4.2
Industrial	6.1	5.4	4.6	4.3	3.7
Other commercial	19.3	-	-	-	-
All Sectors	9.4	6.8	5.1	5.1	4.1

Table 1.2 : Average Lease Length - IPD ERV Weighted - to lease expiry or first break

	Large	Medium	Small	Micro	Unknown
Retail	14.4	11.5	7.0	7.3	5.5
Office	13.3	7.3	5.6	6.3	4.9
Industrial	11.8	7.2	5.7	5.7	4.8
Other commercial	23.8	-	-	-	-
All Sectors	13.8	8.8	6.2	6.6	5.3

Source: Investment Property Databank

However, in the process by which leases are negotiated, noticeable differences do occur between the very small micro business (in the UK defined as a business with less than 10 employees, see Chapter 3) and other small business (up to 49 employees), even though their lease lengths do not differ greatly. A significant number of very small micro business tenants take no commercial advice when negotiating leases even though many of them have no prior experience of taking leases; and the smaller the business the less likely they are to take advice.

Despite the differences between the behaviour of very small micro businesses and the others, and that small business tenants are one of the three main items on the Government agenda for leases, at no time has the UK Government hinted at legislation for small business only. The legislative option across the whole market still remains and most Government threats to use it have been to address single issues, rather than an comprehensive Act which could address both the individual items in a lease and the process by which leases are negotiated.

In some other countries, legislation to control the landlord and tenant process has been the option adopted and that legislation does not cover the whole market. One such country is Australia. It may be that many of the issues concerning small business are shared between the UK and Australia and this research therefore examines the nature of the legislation in Australia and the cultural, political and market context in which it operates. Much of the legislation in Australia dates back to the early to middle 1980s and has had a 20-year gestation period in which to develop. It gives ample time and opportunity for more difficult issues to be isolated and examined with alternative solutions tried and tested.

Due the federal system in Australia, the individual States have significant powers in certain areas and leasing is primarily a State rather than a Federal issue. This complicates the issue with different legislation enacted in different States leading to different processes in different States. However, they all have the common factor that the legislation is partial across the market and not all tenants are included; and individual tenants can be included in one State's legislation but not included in another's legislation. Therefore, rather than study Australia as a whole, the main field-work has been carried out in one State, Victoria. However, an overview of the legislation across Australia is included in Chapter Three with the main case study of Victoria being included in Chapter Four. Chapter Two sets out the main aims and objectives and the approach to the research. Chapter Five concludes by drawing together the implications of the findings concerning the Australian legislation for the UK commercial leases policy debate.

Chapter 2 – Research Aims and Methods

2.1 Aims and Objectives

The aim of the research is to examine perceptions of the effectiveness of small business tenant legislation in Australia and to provide a preliminary evaluation of its potential use in UK.

The objectives are to:

- Identify the policy aims and objectives of small business tenant legislation.
- Determine the nature and scope of small business tenant legislation in the Australian States in terms of the identification and classification of small business tenants and premises and examine the different strands to the legislation and how they are perceived to impact on the landlord and small business tenant relationship.
- Identify the perceptions of stakeholders in the Australian leasing market and evaluate the perceived effectiveness of the legislation in the context of the policy aims and objectives.
- Discuss the possibility of similar legislation being applied to the UK and provide a preliminary conclusion on the advantages and disadvantages with this option.

2.2 Research Methods

First, the aims and objectives have been addressed by reviewing the relevant literature and legislation in Australia in general and Victoria in particular. The legislation in Australia has been the subject of a significant amount of comment and review and generated a substantial literature. Given that the objectives and time frame of this research are relatively confined, this report will only set out the main issues from that literature as they relate to the UK small business awareness policy research question.

Second, the overview of the literature and legislation was used to identify the issues developed within a set of semi-structured interviews with a combination of Government, property professionals and representatives of landlords and tenants. In total 28 individual interviews were carried out in March and early April of 2006 with 36 interviewees (a number of firms and organisations fielded two or more individuals). The interviewees are listed in the acknowledgements along with other contacts who, while not part of the formal interview process, provided information on data and other issues related to the research.

The interviewees included 9 lawyer representatives of professional law firms and 16 representatives of letting agency practices and property valuers, operating for both landlords and tenants. Two representatives of the Retailers' organisations for Victoria and New South Wales and a representative of the Australian Council for Shopping Centres were interviewed along with a major shopping centre owner, a major financial institution and a major retailer. Government interviewees included the Government official responsible for organising the drafting of the 2003 Victorian legislation, the Small Business Commissioner and 2 representatives of his office who

organise the mediation of disputes under the legislation and the Valuer-General for the State of Victoria.

In addition, a meeting with the Commercial Leases Committee of the Law Institute of Victoria was arranged to discuss the issues and the researcher also spoke and invited questions at two continuing professional development seminars, one for valuers arranged by the Australian Property Institute and the other for lawyers arranged by Legalwise, a law CPD institute.

Finally, empirical lease data on rents, lease term, rent review, repairs and renewal rights was sought but it was found that the data did not exist in a similar form to that in the UK. In some States lease data is registered but is only accessible individually for a fee. The Investment Property Databank exists in Australia but its performance measurement dataset does not include leases. However, Property Investment Research, a private firm, collect property market data and had a small sample of leases which has been analysed in Chapter 3. One anonymous source did release two case studies of Victorian shopping centre lease schedules and these are analysed in Chapter 4 to give some context of the discussion on leases and lease terms throughout the rest of this research.

Chapter 3 – Development of Small Business Tenancy Legislation in Australia

3.1 Introduction

This chapter sets out to briefly describe the development of the most recent landlord and tenant legislation aimed at small business in Australia and identify the different provisions of the different States and Territories. There are a number of general issues which impact on the research and these are also set out in this chapter.

First, the Federal system of Government has implications for the development of the legislation. Australia's federal system incorporates eight States or Territories; these are New South Wales, Victoria, Queensland, South Australia, Western Australia, Northern Territory, Australian Capital Territory and Tasmania. Each of these has individual responsibility for landlord and tenant legislation. The Federal Parliament is called the "Parliament of the Commonwealth of Australia" and in this report Australian Commonwealth or Federal Government refers to the Government of Australia while State Government refers to the Government in one of the eight individual States or Territories. The role of the Australian Federal Government and the States must therefore be understood to put any legislation in context.

Second, the debate and legislation normally refers to retail tenancies rather than small businesses and this raises issues of what the legislation actually covers. The reason for researching Australia is to find out how they deal with the awareness of small business tenants but there is no guarantee that the legislation actually refers to small business tenants, even small business retail tenancies.

Third, there are also other legislative influences on the landlord and tenant relationship, not least the unconscionable conduct provisions of the Trade Practices Act 1974 being incorporated into retail tenancy legislation.

The data in the public domain in Australia on leases is in many respects very poor. There is registration of leases in NSW. However, even though the main providers of private UK lease data Investment Property Databank are present in Australia and the Property Council of Australia have been collecting performance measurement data for well over 10 years, there are no databases where the mass data has been analysed to give sub-sector specific details of leased length, review patterns and types, and other lease terms.

One small sample of properties from across different sub sectors of the market from all over Australia provided by Property Investment Research (PIR) consists of 124 properties which have an average lease length of 9 years. They include 64 retail, 48 offices and 12 industrial properties and the average lease lengths are 9.4 for retail, 8.4 for offices and 8.8 for industrial.

However, the distributions suggest little conformity over the market as a whole although 5 and 10-year leases do represent over 25% of the total. But as Figure 3.1 illustrates, while retail has one third of the leases at 15 years or over and nearly 20% at 10 years and another 20% at around 5/6 years, offices lease lengths cluster between 5 years and 12 years.

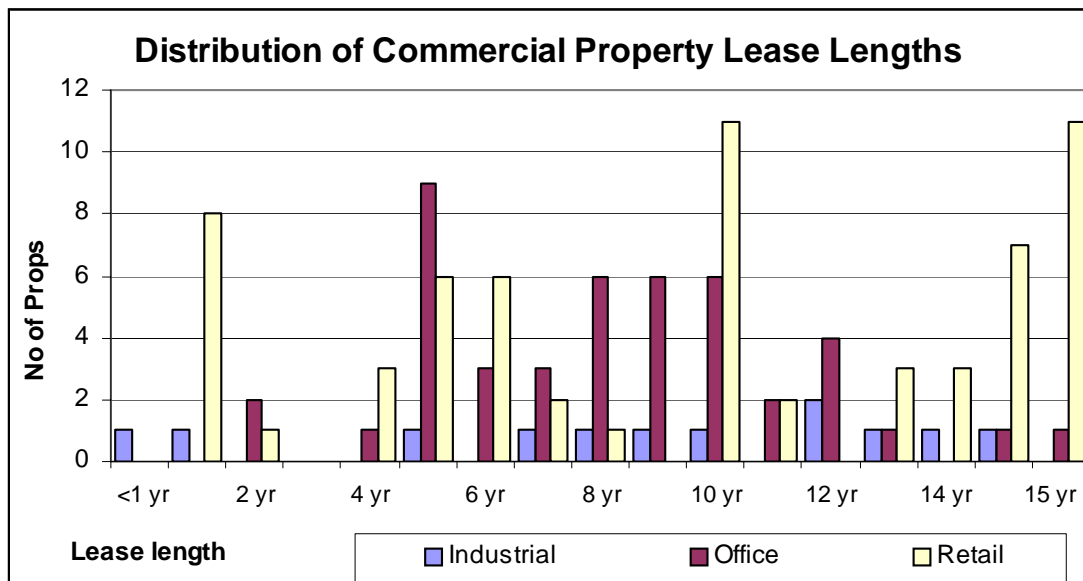


Figure 3.1 Distribution of Commercial lease Lengths
Source : Property Investment Research (PIR)

The retail rent review type is described as ‘base plus turnover’ in 90% of cases while the most numerous review type for offices is based on fixed increases in over two-thirds of leases.

In addition to the above, tenancy schedules of two shopping centres in Victoria were obtained from a confidential source and will be set out in the next chapter dealing with Victoria.

3.2. The Genesis of the Legislation

The catalyst for Government action in the landlord and tenant relationship leading to legislation is fairly well established in the literature and it is laid firmly at the door of the major shopping centre landlords. They are accused of behaving badly and certain landlords are named frequently by commentators and interviewees.

The main criticisms were re-iterated in the Beddall Report (1990) and seem to be based on two main issues, rent and outgoings. Due to the physical nature of Australian shopping centres, where major regional centres are planted in the middle of suburban areas and accessed by car, there appears to be little scope for the retailer who lies outside the centre. This is in contrast to many in-town centres in the UK where the streets just outside the centre still generate good pedestrian flow. Strip shopping immediately outside many of the large Australian centres is convenience and low value with little pedestrian flow.

The retailers accused the landlords of shopping centres as creating an “autonomous” or monopolistic market and charging unaffordable rents. They also accuse landlords of charging inappropriate outgoings. The shopping centre owners answered by claiming that high occupancy and high renewal rates prove that retailers are doing

well and it is the location in the centre which provides them with the appropriate premises. It is not the purpose of this report to investigate the past or present claims of either side of this argument but the fact that State Governments have all, at various times, seen fit to legislate suggests that they all believe an imbalance exists between the negotiating power of landlords and tenants. The Beddall Report (1990) seems to sum up the past and current perception. “The committee considers that the disparity in bargaining power between small retailers and a shopping centre landlord can result in a landlord abusing his more powerful position by including unfair conditions into leases offered to smaller retailers”. Actual incidences of these abuses were elicited from some of the case study interviews and will be reported in the next chapter.

The first legislation was enacted in Queensland in 1984, Western and South Australia followed in 1985 and Victoria in 1986 (Davies, 1991). As indicated above all other States have now followed. One important question for the UK policy debate is the role of voluntary codes. New South Wales did go down the route of a voluntary code although the 1991 voluntary code was adopted after 3 years of unsuccessful negotiations to develop a mandatory code (Carkagis, 1997). Despite both shopping centre landlord and retailer organisations’ support, it was not adhered to and in 1994 New South Wales also enacted legislation after it was decided in 1993 that the voluntary code had not worked (NSW Hansard, 1993, 1547-8). In introducing the Bill, the New South Wales Minister for Small Business, Mr Chappell, suggested the main policy reasons for intervening in these particular commercial agreements are to ensure agreements are explicit as to the requirements of each party, entered into from a position of reasonably equal negotiating strength and to provide a cost effective and timely dispute resolution process (NSW Hansard, 1993, 1547).

Table 3.1 sets out the current legislation in each State.

Table 3.1 : Australian State/Territory Legislation

State	Name of Act	Date of Commencement	Last Amended
Australian Capital Territory (ACT)	Leases (Commercial and Retail) Act 2001	1 st July 2002	4 th March 2003
New South Wales (NSW)	Retail Leases Act 1994	1 st August 1994	1 st January 2006
Northern Territory (NT)	Business Tenancies (Fair Dealings) Act 2003	1 st July 2004	
Queensland (QLD)	Retail Shop Leases Act 1994	28 th October 1994	April 3 rd 2006
South Australia (SA)	Retail and Commercial Leases Act 1995	30 th June 1995	6 th December 2001
Tasmania (TAS)	Fair Trading (Code of Practice for Retail Tenancies) Regulations 1998	1 st September 1998	
Victoria (VIC)	Retail Leases Act 2003	1 st May 2003	23 rd November 2005
Western Australia (WA)	Commercial Tenancy (Retail Shops) Agreements Act 1985 incorporating the Commercial Tenancy (Retail Shops) Agreements Amendment Act 1998	1 st September 1985 1 st July 1999	28 th June 2001

Sources: Compiled from primarily Philips Fox (2004), Clayton Utz (2005), Minter Ellison (2006)

3.3. National v State Legislation

Although there have been a number of calls for a consolidation of the legislation across the Commonwealth of Australia (see, for example, Beddall Report, 1990; Reid Report, 1997; Baird Report, 1999; Cameron and Blom, 2004), this has not occurred. As retail tenancy matters are a State not a Federal responsibility, the powers would have to be referred from the States.

In response to the 1997 Reid Report, the Federal Government set out its reasons for declining to intervene on the grounds that the “Federal Government has only limited constitutional capacity to legislate with respect to retail tenancies” but supports the idea of equity “across the retail sector” (response of the Minister – Commonwealth Hansard, 30th September 1997, page 8768). Two years later, the Baird Report (1999) expressed its concern that the Federal Government had not taken on board the Reid recommendations concerning a uniform retail tenancy code as Baird still perceived an imbalance existed between the landlords’ information base when setting rent compared to the tenants. Again the Federal Government declined to intervene on the grounds that retail tenancies were a State not a Federal matter, but suggested that it had elicited a promise from all State governments in December 1997 to introduce minimum standards on disclosure of information at negotiation, rent reviews, ratchet

clauses (upwards only) relocation expenses, outgoings and assignment. This, they claimed, had occurred, apart from in the NT which was then in the process of developing its legislation.

Davies (1991) addressed the issue of uniformity and concluded that the advantages of a uniform system were that landlords would find it more difficult to play off different States against one another to achieve regulatory concessions and that tenants would stand a better chance of equity no matter what State or Territory they were operating in. If the former were true, then you would not expect the shopping centre industry to ask for consolidated legislation but Cockburn (2005) has criticised the lack of conformity in retail tenancy legislation, even though he acknowledges that national legislation is now not likely to emerge. Webb (2006) observed that the two pivotal recommendations of the Reid Report, the uniform lease code and a statutory prohibition of unfair conduct in small business transactions, have still not been enacted 10 years later.

There is no sign of the States referring the power to legislate to the Federal Government. The States appear to have a vested interest in keeping the individual legislation in that national legislation may adopt a lowest common denominator effect and the States with, in their opinion, the strongest or best legislation may lose the intellectual capital invested over the last 20 years in developing it. Davies (1991) saw the only disadvantage of a common approach as the cost, disruption and possible confusion associated with changing the status quo in those States where the legislation had already been enacted. This predates the plethora of revisions and re-enactments within many States since then. One issue identified by Cameron and Blom (2004) which could be seen as either an advantage or disadvantage is the continual leapfrogging of States as they attempt to take the best bits of others' legislation and remove the bits that do not work so well. While this could lead to better legislation and more conformity, Cameron and Blom (2004) imply that it is more political than technical. This can lead to more frequent change and more inconsistency and therefore much greater compliance costs for both landlords and tenants. They identify possible inconsistencies within definitions of which property and which tenants are included, treatment of rent review type, treatment of outgoings and implied obligations on landlords.

On the surface, the issue of Federal and State Government is not an issue for the UK. However, this may not be completely true. The Landlord and Tenant Act 1954, the major piece of legislation regulating the landlord and tenant relationship, applies to England and Wales only and not Scotland or Northern Ireland. As it only controls the renewal process it also has a very specific effect. If more legislation were enacted would it be for England and Wales only and would it create some differences between different parts of the UK? It could add to compliance costs in one area but not others. However, most national and international landlords and tenants are already used to different systems in different markets and are used to adapting to the different regulatory regimes. Interviewees who acted nationally did not see this as a major problem, rather an irritant as indicated earlier in this Section.

3.4. Small Business or Small Retail Tenancy Legislation

The comments above also raise another issue for the UK policy debate. The legislation largely refers to retail tenancies and the UK awareness of small business tenant agenda is not confined solely to retail. Therefore there are questions of why the Australian legislation appears to be aimed at retail alone and office and industrial tenants do not warrant similar protection.

Obviously, as the catalyst for the legislation was the perceived imbalance between shopping centre landlords and smaller tenants, the discussion and the subsequent legislation have built up around small business retail occupiers, but defining this group has caused problems for legislators which will be discussed more fully below and in Chapter 4. Depending on a more detailed investigation of what the actual policy objectives in Australia are and whether they are truly to protect small business retail tenants (again discussed more fully in Chapter 4), a legitimate question is whether all small business tenants are vulnerable to imbalances in any system. In the UK, there has been no discussion of legislation aimed at one section of the community only so far. So all questions remain open; should there be no legislation, legislation aimed at part of the market (either small business, small retail or even all retail) or legislation aimed at the whole market. In Australia, the same questions could be asked. On the surface it is small business retail legislation although this is an historic policy position from the problems of the 1970s and 1980s.

3.5 Issues Covered by Legislation

Three major firms of lawyers in Australia, Minter Ellison (2006), Clayton Utz (2005) and Phillips Fox (2004), have produced compendia of the retail legislation across the eight States and Territories of Australia and the Minter Ellison report is attached as Appendix One of this report with the kind permission of the authors. These compendia, which are available free from each of the respective firms' websites, illustrate the extensive nature of the legislation and the issues covered by it as well as the similarities and differences between the legislation in the individual States and Territories. Phillips Fox include 28 issues, Clayton Utz 37 and Minter Ellison 60. Table 3.2 categorises the issues covered by the Acts into six main categories. In addition to the prescription of actual lease terms, the process by which the lease is negotiated and the relationship between landlord and tenant after the lease commences are also covered by the legislation.

Table 3.2 - Major Issues Covered by the Retail Leases Legislation

Major Category or Issue	Issues within Category
Premises or tenants within the Acts	Definition of premises Definition of tenants Definition of who or what are not included
Provision of information during and after negotiations	Provision of draft leases and other information Disclosure statements by landlords and tenants Termination rights from failures to deliver information and disclosure statements Notification/registration of leases
Financial and other terms of the lease	Implied terms Regulation of actual terms such as rent, rent review, outgoings, sinking funds, assignment, subletting, minimum term, refurbishment, renewal rights where they exist, relocation.
Dispute resolution	Role of Courts Mediation systems Role of registrars and small business commissioners Valuations Confidentiality of proceedings and evidence
Unconscionable conduct	Incorporation of unconscionable conduct into Retail Leases Lists of behaviour that might be construed unconscionable.
Other issues	Key money, compensation to tenants, trading hours, security deposits, personal guarantees, land and sales tax provisions, payment of rent during fit out, management fees, advertising and promotion.

These major issues form the basis for a discussion of the approaches taken to each of them by the different States and Territories

3.5.1. Definition of premises and tenants

The definition of small business or small business premises is a major issue for the introduction of partial legislation across a market and the problems associated with it are amply demonstrated by the various ways in which the different jurisdictions in Australia have attempted to solve it. The issues relate to defining both premises and tenants.

In most States the definition of what comes under the Act is based on the premises alone and two basic approaches have been used, occupancy cost and floorspace. In VIC and SA the basis is occupancy cost while in WA, QLD, NSW, TAS, ACT and NT it is based on floorspace. The floorspace criteria for inclusion within the Act is

less than 1000 square metres in all of the six States apart from QLD, which is 10,000 square metres unless it is let to a public corporation and then it is 1000 square metres. The occupancy cost limit is A\$1,000,000 pa in VIC and A\$250,000 in SA. The debate concerning the use of costs or floorspace will be examined within the case study of Victoria.

All shops within these rent and floorspace limits in a shopping centre are normally included and most States define a shopping centre in the legislation as a cluster of at least five shops in the same ownership. But other retail premises are also included in the legislation and need defining. In attempts to remove inappropriate occupiers or users, various inclusions or exceptions are listed. For example in NSW, a list of users is included in the legislation (Appendix Two) and this list includes restaurants and cafes but does not appear to include service providers such as valuers, estate agents and lawyers operating out of traditional high street premises. However, in other States this kind of use is specifically included under a wider definition of retail which includes retail services and in ACT, VIC and SA some commercial premises are included if they fall within the rent limits or, in the case of ACT, have an area of less than 300 square metres or, in the case of VIC, are located only on the ground, first or second floors. In some States exclusions from the Act include very short leases of less than 6 months or some long leases of 15 years (VIC) or 25 years or more (NT, NSW), in others certain types of retail outlet are excluded such as those in certain listed leisure outlets (TAS) or where the shops within the leisure outlet are run by the leisure outlet proprietor (NSW).

The nature of the tenant can also come into the equation as many tenants of shopping centres occupying floorspace of less than 1000 square metres at less than the prescribed rents could be major national or international companies who do not come under the definition of small businesses. In the UK and Australia, a small business is defined for statistical purposes by the number of employees (see Table 3.3).

Table 3.3 - Definitions of Small, Medium and Large Enterprises in Australia and the UK.

	Australia	UK
Non Employing/Micro Business	0 - 4 employees	0 – 9 employees
Other Small Business	5 - 19 employees	10 – 49 employees
Medium Sized Business	20 - 199 employees	50 – 249 employees
Large Business	200 or more employees	250 or more employees

Sources - UK Small Business Service of the Dti and Australian Bureau of Statistics

However, these criteria are not used in retail tenancy legislation. Instead, in VIC, where the premises do not form the whole basis of the legislation, the type of company is used rather than its size by number of employees or turnover figures. Tenants who are listed or are a subsidiary of a listed company on the Stock Exchange are excluded from the Victorian Act. In past legislation VIC has operated a definition based on floorspace and so has experience of all the different approaches to defining what comes into and what is excluded from the Act. These issues will therefore be revisited in the next chapter including the issue of certain tenants who are included in one State and excluded in another.

3.5.2 *Information and disclosure*

There is an element of conformity concerning the information provision at the commencement of negotiations across the States. A copy of the proposed lease must be given to the tenant or made available for inspection at the commencement of negotiations or soon after in VIC, TAS, SA, NSW, ACT and NT. In VIC and QLD, it must be provided at least 7 days before the lease is signed and in WA it must be given along with the disclosure statement. This is in stark contrast to the findings of Crosby *et al* (2005) in the UK where, at the commencement of negotiations, a prospective small business tenant was likely to be informed of only the proposed rent with other terms by negotiation. Even at the end of the commercial part of the negotiations a short set of heads of terms would be agreed and sent to the lawyers to subsequently draft the lease. Non-compliance with the information provisions can lead to fines in some States; A\$5,000 in VIC, A\$500 in SA and A\$5,500 in NSW.

In addition to a copy of the proposed lease, some States require that landlords give out Government guides, codes or approved handbooks to tenants, for example VIC, TAS, WA, ACT and NSW. The NSW brochure (RTU, 2006) is produced by the Retail Tenancy Unit of the Department of State and Regional Government and runs to 6 pages of information about setting up a lease, leasing costs and issues that may arise during and at the end of the lease. These brochures could be construed as being similar to the Code of Practice in the UK and in TAS the legislation is in the form of a mandatory Code of Practice which has to be given to tenants as early as possible in the negotiations. This raises the question of whether this information makes small business tenants more aware or obtain the correct advice in time, especially those entering lease negotiations for the first time. In the UK there is no obligation on the landlord or their agent to give the Code of Practice to the tenant at the commencement of negotiations.

Before the lease is signed a disclosure statement has to be sent by the landlord to the tenant. The statement in the ACT must be given at least 14 days before the lease is entered into on the prescribed form. In NSW it is at least 7 days before. It is also 7 days in NT, QLD, TAS, VIC and WA. In SA it must be given before the lease is signed. In many States tenants have the right to terminate the lease if the disclosure statement is late or does not appear and other sanctions include compensation and the ability to withhold rent. The dates for terminating the tenancy vary as do the rights to compensation but all States have given the tenant the possibility of walking away from a signed lease if full information is revealed late or not revealed at all.

Disclosure statements are on standard forms and given the range of different lease and property types, this can cause problems. Both the QLD and NSW disclosure statements run to 6 pages for the lessor. Typical information includes detailed information on terms of the lease with particular emphasis on rent determination provisions and outgoings and, in keeping with the original problems that precipitated the legislation, there are additional questions for occupiers of shopping centres. In the NSW disclosure statement they are 2 of the 6 pages.

In NT and NSW tenants are required to give disclosure statements back to the landlord within 7 days of receiving one from the landlord. In QLD the landlord can request a tenant to give a disclosure statement. All three are on prescribed forms.

However in contrast to the landlord's 6 pages in NSW it runs to one page only. Basically it is an acknowledgement of receipt of the landlord's statement and that the landlord has provided the copy of the draft lease and brochure. It also asks whether the tenant took independent advice and the tenant is asked to make a declaration that they will be able, based on their own business projections, to pay the rent and outgoings under the lease. Finally they are also asked to declare that, in entering into the lease, they have relied upon the information in the lease and the information on the landlord's disclosure statement. In addition there is a space to record any additional verbal commitments or written statements made by the landlord or their agents that they declare they have relied upon. In the early Victorian legislation, tenants were required to produce a business plan as their disclosure statement, which had some legal implications but could ensure they had a better planned business model prior to taking the lease.

Disclosure statements are also an issue upon assignment and subletting and there are provisions in each of the Acts concerning the provision to the tenant of signed copies of the lease within prescribed time limits. However, some States are silent on what happens if these provisions on the delivery of the lease are not met.

3.5.3 Terms of the lease

The legislation in all States has detailed provisions prescribing terms of the lease. These provisions have a large number of similarities in that the same types of issue are addressed across all States, even if the detail sometimes differs. Total costs of occupation figure prominently in the legislation due to their role as one of the most controversial aspects of the relationship in the 1980s. These costs can be categorised within rent determination, rent review and other costs of occupation such as outgoings. All of the legislation, except for the code in TAS, defines outgoings and they normally include annual maintenance and repair of the building as well as rates, taxes, levies and premiums. The legislation also addresses liability and apportionment and outgoing information exchange. It also usually addresses issues of liability for letting fees and management costs, land tax and promotion and advertising fees. Because of the concentration on retail in shopping centres, the legislation also focuses on key money, turnover rent and rent determination at review and renewal.

Key money is defined in the legislation in all States and usually the definitions refer to payments that are to procure the grant, extension, renewal or assignment of the lease by the tenant to the landlord. Generally landlords cannot seek or accept key money payments as defined from tenants. Where fines can be levied for a breach, they range from \$1,000 in TAS to \$11,000 in NSW.

Turnover rents require careful regulation and the legislation has to define in detail what the definition of turnover actually includes or excludes and the legislation across all States is similar in that around 12 items are specifically excluded; for example, discounting, losses on resale, uncollected accounts, refunds, taxes, delivery charges, sales of fixtures and fittings and lottery sales. Turnover figure confidentiality is also dealt with under the legislation in all States. Landlords cannot divulge tenant turnover without the tenant's consent except under certain circumstances; to courts and business commissioners for dispute resolution and to their advisors. They can divulge

aggregated figures for the centre as a whole and in some States, they are not able to get tenant turnover figures unless they relate specifically to the rent determination process. In all States except QLD and WA, any clause that seeks to terminate the lease early if certain turnover targets are not met is void.

Rent reviews also attract detailed consideration. In many States the basis of review must be specified and reviews cannot be more frequent than every 12 months. The allowable bases of the review are specified in VIC, QLD, TAS, and NT and in many States no more than one basis can be adopted (for example, a clause suggesting the higher of 2 bases is void). All States have effectively banned an upwards-only rent review or a review where the fall is capped. They have all defined market rent and the rent determination process to obtain market rent and that normally requires a specialist retail valuer to be appointed, that appointment being made independently if the parties cannot agree. In some States that is by retail or business commissioners in others by the Australian Property Institute, the major valuer's professional body in Australia.

A minimum length of lease of 5 years is prescribed in all States except QLD. However, in the majority of States there are exclusions including the right to contract for less than 5 years if it has been approved by retail or business commissioners or certified independent legal advice has been taken. Leases of less than 6 months are also often excluded and subleases cannot extend beyond the head lease expiry date.

A right of lease renewal is not generally available in the legislation. The exceptions are SA and ACT where preferential renewal rights exist. These first refusal provisions are restricted to shopping centre tenants. However, the rights can be contracted out with the signing of a certified exclusionary clause in both SA and ACT. In addition it can also be frustrated in ACT if it would be substantially more advantageous for the landlord to lease the premises to another tenant or if they wanted to change the tenancy mix.

Outgoings, as previously indicated, are defined as annual maintenance and repair of the building as well as rates, taxes, levies and premiums. In all States, leases must specify how the amounts are to be calculated, how they are to be shared out between different tenants and when they are to be recovered. All States have a list of prohibited items and the kinds of item which appear regularly include depreciation (sinking funds) and any item which is not specifically related to the tenant's unit. The collection of land tax is specifically dealt with in all States except TAS and NT but the charging of management fees is only mentioned in 3 States, but only WA prohibits it. Centre promotion and advertising can be claimed from the tenants but only under strict guidelines in each State. In addition, the legislation in various States deals with a raft of repair and maintenance issues such as initial fit out (all but QLD, TAS and WA), notices of work, damaged premises, refurbishment (all but QLD and WA), urgent repairs (VIC) and compensation for disturbance (all States).

Assignment and subletting is also controlled in all of the legislation. Absolute prohibition of subletting appears to be allowed in most States except ACT but not absolute prohibition of assignment. The process is controlled through the legislation in all of the States and all but QLD must give consent unless certain grounds for refusal are met, usually based around a non-permitted use or the proposed assignee

being not of a sufficient financial standing. Disclosure statements from landlords, assignors and assignees are an issue at assignment as well as at the granting of new leases in some States, for example QLD, NSW, SA, and VIC.

Overall, parties to leases that come within the legislation are not free to negotiate many terms of the lease. There are restrictions on the length of leases, types of rent revision clause and what can be included in the rent and in service charges. There are also restrictions on assignment and subletting. Of particular interest to the UK is the ban on upwards only rent reviews and the effect that this has had on the type of reviews within leases. This will be addressed in the next chapter when a set of shopping centre leases will be analysed for length and review type. In addition, it is also interesting that an absolute ban on subletting appears to be allowed in the majority of Australian States. As this is the lead issue in the UK following the latest Government review in 2005, it is interesting to note that, at the time that the most likely target of UK Government intervention will be subletting, it is virtually untouched by the Australian legislation. In Victoria, the latest legislation has increased the landlord's rights to ban subletting and the reasons for this movement warrant scrutiny when the case study is undertaken.

3.5.4 Dispute resolution

Dispute resolution procedures are lengthy in each of the Acts so only an overview is provided here. However, where the Acts apply, there is a common theme and that is the use of a process which tries to give a cheaper and easier route to a settlement than the escalation of the dispute straight from negotiation to courtroom. Although the acts have different processes the common theme is the use of registrars or commissioners and mediation. This occurs in VIC, QLD, TAS, SA, WA, NSW and NT.

In the ACT, the magistrates court has the power to assess what the best way of settling the case might be and can order a case management meeting. In VIC there is an Office of the Small Business Commissioner which runs the mediation system and before a case can be brought before the courts it has to have been the subject of mediation within that office. In NSW, parties can refer disputes to the Registrar of Retail Tenancy Disputes who has the power to intervene in court proceedings. A similar system is in place run by the Commissioner of Business Tenancies in NT. Mediation is not compulsory in WA, SA or QLD but the courts can refer the dispute to the Commercial Registrar in WA, the Commissioner for Consumer Affairs in SA and a Chief Executive in QLD. In TAS, either party to a dispute can refer the matter to the Office of Consumer Affairs who attempt to resolve it. If that fails, there is a Monitoring Committee of the Code of Practice which attempts to conciliate. If that fails it is referred to the Courts. In all the other States there is only one mechanism to mediate before it goes to the relevant court or tribunal for adjudication.

The process raises a number of questions for the UK. Apart from alternative dispute resolution, the role of the registrars or commissioners in the process is worthy of investigation for how effective they are at settling disputes. Are they quicker, cheaper and more effective than the direct route from negotiation to court more common in the UK or are they an added level of bureaucracy which adds to the cost and time of settling disputes? The case study of Victoria will therefore investigate the role of the

Small Business Commissioner who has responsibility for organising the dispute resolution process in that State.

3.5.5 *Unconscionable conduct*

Unconscionable conduct is a concept which according to Reid (1997) is used to describe “conduct by a party which stands to receive a benefit from a transaction which, in good conscience, should not be allowed to stand”. Although unconscionable conduct is typically the use of or insistence upon certain legal rights under contracts, it can also be the use of superior bargaining power in creating the contract. The relevant doctrines are unconscionable bargains, caused by a lack of understanding or legal advice for one party, undue influence from a special relationship and economic duress caused by a lack of practical alternatives. However, a mere presence of inequality is not proof of unconscionable conduct; it has to be shown that one party has taken advantage of the inability of the weaker party (Reid, 1997).

The application of these three principles to lease negotiations in the UK is obvious given the findings of Crosby *et al* (2005) concerning the lack of awareness of small business tenants and their tendencies not to take advice. Its application in the Australian context is equally obvious given the situation of the 1970s and 1980s which led to the introduction of lease legislation in the first place.

The Beddall (1990) report into small business in Australia recommended that the Trade Practices Act (1974) provisions (Section 52 A) applying unconscionable conduct to consumers be extended to include small business transactions including retail/commercial tenancy agreements. They considered that the disparity in bargaining power between small retailers and shopping centre landlords could result in abuse of the more powerful position by including unfair provisions in leases. Davies (1991) suggested that the incorporation of the Trade Practices Act provisions into retail lease legislation would have little effect as most tenancy disputes did not have unconscionable conduct as the root cause of the dispute. Reid (1997) also noted a more general lack of precedents concerning successful cases which could determine principles for identifying unconscionable conduct.

In 1997, in what Redfern (2003) reports was perceived to be a ground breaking policy decision, Section 51AC was added to the Trade Practices Act 1974. This extended the unconscionable conduct provisions to the small business sector and retail tenancies come under those provisions. Duncan and Christensen (1999) called it an “Exocet” in retail leasing. In the following year the Commonwealth (Federal) Government passed the Trade Practices Act 1998. The States then proceeded to incorporate unconscionable conduct provisions into their legislation. NSW was the first to incorporate Section 51AC of the Trade Practices Act into their legislation followed by QLD.

Apart from WA, all States now have reference to unconscionable conduct in their retail lease legislation. In VIC, QLD, NSW and NT, the reference is to unconscionable conduct by either party. In TAS, the words harsh and unjust are added to unconscionable and in ACT harsh and oppressive are added. In SA, the word used is vexatious rather than unconscionable.

In WA, the Retail Shops and Fair Trading Legislation Amendment Bill is currently (July 2006) before Parliament and if enacted in its present form would amend the 1985 legislation to prohibit unconscionable conduct by landlord or tenant (Minter Ellison (2006)). This will mean that all retail lease legislation within Australia will have unconscionable conduct provisions.

In five States, NSW, VIC, ACT, NT and QLD, there are lists of factors to be taken into account when assessing whether conduct is unconscionable and these include, amongst others, relative bargaining power, whether the other party could understand any documents to the lease, the use of undue influence, the cost of an equivalent lease, consistency of conduct, the requirements of any industry code, failure to disclose future intended conduct, willingness to negotiate lease terms including rent and the extent to which the parties acted in good faith or honestly. In TAS only two items are specifically mentioned, threatening to subsidise a competitor in nearby premises and threatening not to renew the lease unless a proposal by the landlord is agreed to or rent in excess of market value is paid. In SA, the Act States that a landlord may not require a premium for a renewal or threaten the tenant to persuade them not to renew or to exercise any other right under the Act.

In some jurisdictions a time limit for bringing a claim of unconscionable conduct is stated in the Acts. The legislation in VIC suggests that a claim must be lodged within 6 years, in TAS and NSW it is 3 years and in SA it is 2 years.

Webb (2006) reviews the operation of the unconscionable conduct provisions and notes that actual contested court cases are few, although tribunal decisions offer some guidance on what would constitute unconscionable conduct in a retail leasing negotiation. In one case in particular it would appear that a threat by a landlord to a tenant who had an outstanding case in court with the landlord that they would not have their lease renewed if they did not drop the action was deemed hard bargaining only, not unconscionable conduct. Not surprisingly, she concludes that the Trade Practices Act Section 51AC cases so far appear to address only the malevolent and overt types of conduct and less malevolent but still unfair conduct, identified by the Reid Report as needing some remedy, would not be touched. Therefore questions remain about whether the unconscionable conduct provisions do protect tenants against landlords behaving badly.

In the UK, various Government and Law Commission reports have acknowledged the unequal bargaining power of landlord and tenant but have done nothing specific to balance that relationship (Murdoch *et al* (2001)). There is legislation protecting consumers in contract negotiations but this was inadequate until the Misrepresentation Act of 1967. Since 1991, the principle that those offering goods or services for sale or hire to consumers are subject to criminal liability for mis-descriptions have been extended to those buying or leasing property. However, the Code of Practice for Commercial Leases is the instrument most directly affecting tenants and it is of course only a voluntary code.

The implementation of wider or stronger controls on the behaviour of participants in UK leasing has not yet entered the debate. This debate has been undertaken more recently within the Government agenda of business flexibility rather than unfairness,

despite the origins of the debate being the unfair impact of upwards only rent reviews in a recession,. However, both concepts of flexibility and unfairness equally apply, especially to the small business awareness agenda.

3.6 Conclusions

This chapter has briefly summarised the development of legislation across Australia to deal with the perceived problems of unequal bargaining power between landlords and small business tenants. The catalyst for legislation was the perceived bad behaviour of landlords and a representative of Westfield, the largest owners of shopping centres in Australia, is reported in 1998 as “discovering” that shopping centre landlords had a perception problem due to the Reid Report evidence and findings the previous year (Webb, 2006).

Due to the concentration on retail in general and shopping centres in particular, the plight of small business tenants in non-retail has not been a major issue; unlike in the UK where the awareness of small business tenants issue covers all small business tenants. Apart from the catalysts mentioned above, there seems no logical reason for this omission but this question is examined in more detail in the next chapter.

The legislation was first introduced in 1984 in Queensland and over the next 2 decades developed in all States and Territories, with most States having gone through a number of repeals, re-enactments and amendments. There is evidence of States going their own way but also keeping a close eye on the developments in other States, creating some elements of conformity but also major differences between States remain.

The lack of conformity has led to several calls for national legislation but the Commonwealth Government has claimed limited responsibility for legislation in retail tenancy matters and has persuaded States to implement minimum standards. In fact, the two central recommendations of the Reid Report which concern the uniform code and unconscionable conduct, have been ignored by the Commonwealth Government. However, they have been taken on by the individual States which have the responsibility and show no signs of giving it up to the Federal Government.

The use of unconscionable conduct could be a major deterrent to landlords wishing to deal robustly with tenants and the unconscionable conduct provisions of the Trade Practices Act have been drawn down into virtually all State retail tenancy legislation, with the exception of WA who appear set to follow. The impact on the good name of the company from an adverse decision could be severe but the chances of such a decision being made appear slight. There is a distinct lack of precedent as to what actually constitutes unconscionable conduct under Section 51AC of the Trade Practices Act but harsh, arguably unfair, conduct has not been deemed unconscionable in the few cases that exist.

The legislation across the States has many similar themes. The reasons for the legislation, definitions of what is covered and what is not covered within the Act, information and disclosure, prescriptive lease terms and dispute resolution, are all present. This brief overview has enabled an equally brief discussion of major issues but in order to provide a greater degree of depth of discussion, a case study approach

of the legislation and how it has developed in one State has been adopted; Victoria. There is no such thing as a typical State as far as retail tenancy legislation in Australia is concerned, and therefore no claim that Victoria enables the study of all of the relevant issues, but the study of one State does enable some more detail concerning the themes outlined above to be obtained and provides more robust data for discussing the application of this kind of legislation to the UK policy framework.

Chapter 4 – Case Study of Victoria

4.1 Introduction

This chapter sets out in more detail the legislation in the State of Victoria (VIC). VIC is located in the South East corner of Australia and is based around the second largest city in Australia, Melbourne. In order to undertake the case study, in addition to a review of Government and other literature from the early 1980s to the present day, an interview survey of professional advisors and representatives of landlords and tenants was carried out in Melbourne and the surrounding area during March and early April of 2006, as detailed in Chapter 2. The tenancy schedules of 2 Victorian shopping centres have also been examined to provide empirical evidence of actual shopping centre lease terms.

Although this chapter investigates the Victorian Legislation in more detail, the aims and objectives of this research are orientated towards policy. With any legislation, there are detailed legal issues continually being debated and litigated and those debates and the case analyses will not appear in this chapter. Those more interested in the minute detail of the legislation are referred to what is undoubtedly the main authority on Victorian Retail Leasing, *Retail Leasing Victoria* by Clyde Croft (Croft, 2006a).

The legislation in VIC has gone through three major metamorphoses, but also a plethora of reviews and amendments set out in Croft (2006a). The Retail Tenancies Act became law in 1986. In 1998 it was replaced with the Retail Tenancies Reform Act of 1998 and finally that legislation was replaced with the Retail Leases Act 2003. Since then minor amendments have been enacted within the Retail Leases (Amendment) Act 2005.

4.2. History and Evolution of the Legislation

4.2.1 *Reasons for the original legislation*

There was no real debate concerning legislation or a mandatory code versus a voluntary code of practice. Like QLD and WA, VIC went straight for legislation in 1986 following debate which was focussed on what would work and what would not work in the legislation. In presenting the Retail Tenancies Bill to the Victorian Parliament in November 1986, the Minister (D.R.White) outlined the process and the concerns which had led the Government to the point of legislation (Hansard, 1986a, p993). It followed election pledges made in 1982 that it would introduce a standard fair lease to be used in all transactions.

Having set out the policy objectives of fostering small business development by maintaining a competitive environment and ensuring small business is not the subject of discrimination, he outlined the development of the major shopping centres. Although this property type had been developed since the early 1960s, there had been a rapid proliferation in the 1970s and this had led to the Government being made aware that unfair leases were a major problem for small business. This confirms that shopping centres were the catalyst in VIC, as they were nationally, but the minister

made a point of noting that the legislation was designed to protect all small retail businesses.

The Minister reported that the legislation was preceded by two discussion reports from different bodies. The first was received in October 1982 and was carried out by the Victorian Small Business Development Corporation. The main emphasis of the report was on retail within shopping centres; no reason is given for this focus. Evidence for that report raised concerns about “abuses” within the landlord and tenant relationship stemming mainly from the terms and conditions of leases and the lack of understanding of the implications of these terms and conditions by tenants. This is identical to the UK policy question of awareness of small business tenants. They also concluded that landlords could be disadvantaged by an inability to enforce reasonable conditions and ensure premises are used properly by tenants.

In this study, the nature of the abuses were investigated within the survey of professionals as a number of interviewees had been involved in practice at the time. A number of lawyers interviewed had been involved with the advisory groups and had helped draft the legislation. The interviewees gave a number of examples of abuses by major shopping centre owners to their speciality tenants, not just small businesses as the interviewees were virtually unanimous that the catalyst was perceived issues with aggressive shopping centre owners and smaller or speciality retail tenants.

Specific abuses identified were the relocation or removal of tenants, especially those who had paid significant sums for a business with a short unexpired lease, not realising that they did not have the right to renew that lease, and the allocation of service charges. Three issues were identified with respect to service charges; first, service charges which had inappropriate items within them such as a depreciation charge; second, where the major anchor tenants objected and refused to pay certain items these were then spread around the smaller tenants making them pay the whole amount between them and third, these items were not fully disclosed before the lease was signed.

Other issues included upwards-only (ratchet) review clauses and repairs issues which were cited as a continuing thorn. Interviewees also related other cases such as the charging of design fees for ensuring the tenant’s fit out conformed with the centre’s specification (these fees were not disclosed before the lease was signed), the making of false claims concerning the centre’s trading and not disclosing imminent works which would disrupt the tenant’s business. These issues have obviously driven the discussion and the legislation to a major extent hence the emphasis on small retail, disclosure, conduct of the parties, specific lease terms and dispute resolution in the legislation and renewal rights in the discussion.

The second report was received from the Retail Tenancies Advisory Committee chaired by Michael Arnold. This report gave guidance on the prospective legislation and in an unpublished report to this committee, (Redfern, 1983) advised that a mandatory standard lease was inadvisable and would be too inflexible to deal fairly with the many different situations that arise. Both the Arnold Committee and the Government endorsed that view but this has not stopped the useful development of voluntary standard leases by, for example, the Building Owners’ and Managers’ Association (BOMA) and the Victorian Law Institute.

Redfern (1983), having investigated UK leasing, raised the right to renew as a major issue but this was not included in the legislation. Redfern (1983) also made another recommendation that was not adopted, and has still not been adopted, although the development of the legislation has moved towards it over the years. This was that he saw no reason to distinguish between different groups or types of occupation. He thought that any legislation should include all tenants and all commercial property types, so eliminating the need to define what was and what was not included. He also suggested that the evidence to the Advisory Committee came from a variety of tenants, not just retail.

As this recommendation was not acted upon, it raises the issue of defining the scope of the legislation. How this has developed in VIC covers most of the discussion points which would arise if the implementation of this type of legislation in the UK was envisaged. The Victorian Minister acknowledged that the scope of the legislation had been a “matter of some controversy” (Hansard, 1986, p995). However, they decided to implement an Act which covered small retail premises up to 1,000 square metres, following the decisions already made in QLD and WA. In his 2nd reading speech, the Minister made a connection between the unit size criterion and the exclusion of large retail tenants, implying that small businesses occupy small spaces.

In addition to the scope of the legislation, the main issues covered by the Bill were listed by the Minister as:

Disclosure statements and cooling off periods,
Key money and goodwill,
Rent fixing and review,
The term of the lease, and
Determination of disputes.

Although there were other issues including repairs, the Minister chose to identify the above as the important areas.

The bill was unopposed by the opposition although they would not have brought it to the Parliament if they had been in power. However, a spokesperson of the Real Estate Institute of Victoria (REIV) is reported to have said that the legislation could affect the supply of shopping centres if “the yields and rental returns are not going to be forthcoming as a result of over-regulation” and this was endorsed by the partner of a major law firm acting for shopping centre owners. “Government interference in the form of additional bureaucratic requirements imposed on developers will only stifle future planning of major retail projects in this State” (Hansard, 1986b, p1286). These comments seem familiar in the more modern context of the UK commercial leases debate where threats of legislation have been answered by property industry suggestions that development, particularly urban regeneration schemes, will be stifled. In hindsight, the history of Australian shopping centre development from the introduction of the legislation until now does not support that particular view.

4.2.2 *Developing the legislation*

Since the original Retail Tenancies Act (RTA) in 1986, there have been two major re-enactments, the Retail Tenancies Reform Act of 1998 (RTRA) and the Retail Leases Act (RLA) of 2003.

In 1991 and 1993, the Victorian Government reviewed the workings of the RTA. In 1991 they considered that the objectives of the legislation were two fold, the codification and reform of legal rights to redress the complexity and inaccessibility of common law and the provision of satisfactory dispute resolution procedures to resolve the asymmetry of costs and benefits arising from the negotiation of enforcement of retail tenancy agreements (DMID, 1991). These seem to be additional policy objectives from those set out in the Parliamentary debate preceding the 1986 Act and also re-iterated by Nathan J in the case of *Wellington v Norwich Union Life Insurance Society Ltd* [1991] 1 VR 333, the protection of small tenants (reported in DSRD, 2001a). The review addressed two major themes. The first was whether legislation was required and if so what form should it take. The review reaffirmed the importance of legislation for small retail tenants but suggested that those tenants would not receive the desired protection unless there was also a strategy of administration and enforcement. The second major theme was the limiting of regulation to the minimum necessary to achieve objectives. The differences between the objectives set out by the 1991 review and those set out by the Minister in the 1986 debates are therefore important as a pre-requisite of deciding whether the objectives can be met by alternatives other than regulation. The review concluded that legislation was the low cost process to achieving the objectives.

In 1993, a State Government working party produced a detailed report with 56 very detailed recommendations of changes to the legislation (Redfern, 1993). In 1995 a significant amendment to the 1986 Act took place which introduced compulsory conciliation as an adjunct to the compulsory arbitration already required under the Act (Croft, 2000a). A settlement rate of between 70% and 75% was achieved by conciliation between 1995 and the introduction of the 1998 Act described in the next section.

In 1997, the Minister for Small Business, Louise Asher, set up a Retail Tenancies Working Party with Wendy Smith in the chair and asked them to examine the rationale for and the effectiveness of the RTA 1986, examine the nature and effectiveness of legislation in other States and advise on amendments to the legislation.

The Smith Report (1997) claimed overall that the original legislation was largely unsuccessful in its aim of protecting both landlords and tenants in the retail industry due mainly to lessees being unaware of their rights, the cost of taking action in a dispute and a general lack of confidence in the processes under the Act. It was argued that all of the recommendations were aimed at ensuring that all information relevant to making an informed decision is available to both parties before the lease is signed and therefore the recommendations on disclosure were more specific than many other recommendations. Education, information and dispute resolution also figured prominently.

In total the report made 15 recommendations which centred around

- an education programme for both landlords and tenants,
- problems with franchising,
- the development of a model ‘Plain English’ lease and an ‘Information Booklet’,
- amendments to the disclosure process including penalties for non compliance and the introduction of a tenant’s disclosure statement,
- changes to the process of obtaining rent, relocating tenants, assessing market rent reviews, charging for outgoings, assignment and dispute resolution,
- compensation for misleading statements, undisclosed changes to the tenant mix and disruptions to trade,
- allowing tenants to undertake urgent repairs,
- joining of trade or merchant’s associations, and
- methods of measurement of the 1,000 metres.

As in previous discussions, the security of tenure issues was raised and the report reiterated the importance of security to small business confidence. A right to a further 5 year term at the expiry of the original term was mooted but was obviously an area of disagreement within the working party, mainly as to which businesses this right would apply.

The response of Government was the new Retail Tenancies Reform Act 1998 which appears to have been based largely on the working party recommendations and the Minister described disclosure provisions as the “teeth and rationale of this Bill”. (reported in Croft, 2000b, xvii). In a Report Briefing to the Victorian Employers’ Chamber of Commerce and Industry on 27th March, 1998, the Minister stated “I think landlords had previously regarded disclosure statements as discretionary, this is a disclosure statement with teeth. ...landlords will not be able to charge rent until the disclosure statement is handed over.” (Reported in Redfern (2000))

The other major development in the RTRA is that it gave jurisdiction for retail tenancy disputes to the new Victorian Civil and Administrative Tribunal (VCAT). VCAT retained the conciliation and arbitration processes introduced in the 1995 amendment to the RTA described above.

In 2001, the new State Government took on its own election commitment to “undertake a comprehensive review of Victoria’s retail tenancies laws” (DSRD, 2001b) and this eventually led to the new 2003 Act.

The process by which the Act emerged is set out in Croft (2004) who indicates that the original Bill had to be shelved in 2002 while an election took place before being re-introduced in 2003 with a few changes. The Parliamentary process was preceded by an extensive consultation which included a detailed Issues Paper in January 2001 (DSRD, 2001a). After assessing the comments received, the State Government issued a further Discussion Paper in October 2001 (DSRD, 2001b). Finally in 2002 it published an Exposure Draft (ORRR, 2002) again asking for comments.

The Government was keen to match the legislation more closely to its policy objectives and to create performance measurement benchmarks for assessing whether

the legislation “has performed” (DSRD, 2001a, p13). The Issues Paper therefore raised two questions. First, what policy considerations should determine the nature and extent of the legislation and second, how to assess whether the current and future laws work.

The interviews with Government officials revealed that out of around 300 responses to the Issues Paper, not one comment was received concerning these questions.

In the subsequent Discussion Paper, the Government set out its general policy principle for intervention in markets which is to keep the intervention to the minimum necessary to achieve policy objectives (DSRD, 2001b). It then set out five policy principles for retail tenancies and these were re-iterated as still driving Government policy in this area in an interview with the Chief Executive Officer of the Department of State and Regional Development in March 2006. These are:

1. Government regulation of retail tenancies should focus on addressing information imbalances and the misuse of market power.
2. Retail tenancies legislation should only protect small and medium sized retail businesses.
3. Government involvement in retail tenancy matters should aim at ensuring that prospective tenants have sufficient knowledge to make an informed business decision.
4. While a landlord has a fundamental right of control over the use of its property, this right does not extend to engaging in unfair business practices.
5. Landlords and tenants should be able to access a low-cost informal dispute resolution forum prior to any grievances proceeding to formal litigation.

The Discussion Paper isolated a number of categories of concern with the 1998 legislation. First, it lacked policy direction and robustness; second, there were considerable drafting anomalies identified by the Law Institute of Victoria causing uncertainty and confusion and third, there was poor understanding of the rights and obligations of the parties through a lack of education and information circulation.

The 20 recommendations of the review were based around five categories of certainty, fairness, clarity, dispute resolution and education. The first four of these had all been identified in the Issues Paper with the education issue raised subsequently in the Discussion Paper as an important instrument for delivering on the other four objectives. Major changes proposed included;

- a scrapping of the 1,000 square metre basis and replacing with a scheme that used rent level and type of company to determine whether it was in the Act,
- a drawing down of the unconscionable conduct provisions of the Trade Practices Act, setting out in the Act minimum standards for individual lease terms,

- creating a Government funded grievance body to mediate, and
- expanding the current reliance on an information booklet by a wider education programme.

Following the Exposure Draft (ORR, 2002) and the false start with the 2002 legislation, the Government passed the Retail Leases Act in 2003 and this 138 page piece of legislation followed the review findings closely in that it introduced a more detailed set of criteria for determining whether leases were inside the Act and introduced a mediation and information service run by the Office of the Small Business Commissioner (SBC). The latest set of amendments are included in the Retail Leases Amendment Act 2005.

4.2.3 Questions arising from the development of the legislation

This review of the development of the legislation in VIC coupled with the review of issues discussed in the previous chapter raise a number of questions concerning the policy and operation issues of retail lease legislation in Australia. One set of policy questions concern the targeting of the Act on retail tenancies only (why not all commercial premises?) and small businesses (why not larger tenants as well?). An all-encompassing act would eliminate one of the major operational issues, defining the scope of the Act and which tenancies are included and excluded.

One major feature of all of the legislation is the information dissemination and disclosure statements by both landlord and tenant designed to create clarity and reduce uncertainty but also to better inform the parties of their rights and responsibilities under the lease. The awareness of small business tenants is the major UK policy issue driving this research so the effectiveness of this facet of the legislation is particularly pertinent to the conclusions of this paper.

Addressing the same issue of awareness is the effectiveness of the education programme for all stakeholders in the landlord and tenant relationship. In VIC, the Office of the Small Business Commissioner has a major role, as do the professional organisations. In addition to his educational role, other responsibilities of the SBC's office in VIC include the operation of the low-cost dispute resolution service and to take proceedings for offences against the Act. The effectiveness of his office in undertaking these responsibilities is therefore another major area of study for this paper.

The insertion of the unconscionable conduct provisions into retail lease legislation across the States has been discussed in the previous chapter. Nothing that has happened in VIC in particular adds to that debate and therefore this issue will not be developed in this chapter. However, in the interviews carried out for the case study, a number of interviewees acted across a number of, or all, States. There was a fairly unanimous opinion that the drawing down of the unconscionable conduct provisions into the retail leases legislation has increased the feeling that an action for unconscionable conduct against a major landlord was a significant deterrent to any temptation to behave very robustly against a tenant. Being cited by the SBC for a minor or even quite major offence against the Act did not have the same brand image

damage attached to it as a citing for unconscionable conduct. So far, as indicated in the previous chapter, few cases have been heard on retail tenancy issues and Webb (2006) feels a case would be hard to prove, but it still remains a major issue for landlords.

Finally, the lease legislation prescribes certain lease terms and, in VIC, Part 4 of the RLA deals with entering into or renewing leases, Part 5 deals with rent and outgoings, Part 6 refurbishment, relocation and other “interferences” with the tenancy and Part 7 deals with assignment and termination rights. In addition, Part 8 deals with other matters of lease terms dealing exclusively with shopping centres. This interference in lease terms runs to 55 pages. Many lease terms are banned with upwards-only rent reviews being of particular interest to the UK. The introduction of legislation has changed the nature of some of the terms negotiated in the property market and a study of the actual lease terms from 2 confidential case study shopping centres in VIC provides some evidence of present day typical terms and the interview surveys add some information on the development of those terms since the legislation was enacted.

4.3 The Scope of the Legislation

4.3.1 Policy considerations.

The DSRD (2001b) discussion paper did address some of the more basic questions that remain unanswered from the review of the development of the legislation across all States undertaken in the previous chapter. The first of these is why has Australian legislation ignored all other businesses other than small retail? In the case of VIC, the Government sees a particular problem with the location specific nature of retail. They argue that location is particularly unique in retail compared to office and industrial and this is even more so in major shopping centres. They state that the location specific nature of retail can lead to a sitting tenant issue with an existing lessee particularly vulnerable to being excluded from the location at lease expiry. As other business uses do not suffer with this issue to the same extent this means that it is only retail that requires intervention, given that the policy is to intervene only when absolutely necessary. It does of course raise the issue of renewal rights; if this is such an issue why not solve it by adopting a UK style right to renew or a strong first preference right backed up by independent valuations upon renewal. The second part of this issue is the concentration on small businesses. The argument here is that small business are most likely to suffer from information imbalances and so under Policy Principle 1 action is necessary to protect them but not larger more powerful occupiers. The legislation is therefore aimed at small and medium sized retail businesses (DSRD, 2001b).

However, in the UK, Crosby *et al* (2005) found evidence that the different behaviour of tenants concerning the lease negotiation process was most marked between small and both medium and large sized tenants. Given that the policy principle is information imbalances there is a question mark over the protection of any other than the smallest business tenants. There was also no difference between retail and office tenants in the UK, which again begs the question of why retail only as all small business tenants need to be better informed. In the UK, the perception was that all small business tenants took leases on the first terms offered, did not get advice before

agreeing to the major lease terms and rent and in some cases took no advice at all (Crosby *et al*, 2005). However, there is no real evidence that information imbalances are being systematically misused in the UK, despite individual cases which obviously arise, although the UK interview survey of professional advisors did feel that unadvised small business tenants did not get the best deal possible (Crosby *et al*, 2005).

The Australian interview survey carried out for this research included questions concerning this issue. A number of interviewees had not addressed the question before, taking the focus on retail for granted as it was embedded in the legislation from the outset and also because the major shopping centre landlords were seen as the catalyst. A few had addressed the question and most of those thought that the awareness issues were an issue for all small business commercial tenants, so they would have difficulty defending the concentration on retail. The consensus was that large tenants of any description did not suffer from a weak negotiating position and that the listed national speciality retail companies were necessary for the shopping centre and could get concessions and lease terms that suited them. However, one major retailer who is within the legislation in some States but not others, suggested that they still had difficulty getting full disclosure of future occupancy costs when not inside the Acts and many aspects of the legislation have benefits for all tenants.

4.3.2 Operational difficulties.

Having adopted a policy stance that distinguishes small business and retail, the interviewees acknowledged that this is a difficult issue to resolve. So much so VIC has changed its approach in the latest legislation from a very crude floorspace measure (adopted by the majority of States) to a more complex formulae based on the type of tenant and the cost of occupation.

With certain exclusions, the Victorian Act does not apply to very short leases of less than 1 year. Leases that have an occupancy cost of more than \$1 million pa are also excluded. Occupancy costs are rent, excluding any turnover element, and tenants' outgoings and any other costs that the tenant is liable for. Tenants which are companies or subsidiaries of companies listed on the Australian Stock Exchange, or any international exchange which is a member of the World Federation of Exchanges, are also excluded. The use of the property also comes into the definition of what is included or excluded; premises predominantly used for or intended to be used for the sale or hire of goods by retail, or the retail provision of services, are included. The Minister can additionally prescribe specified businesses, premises or tenants by notice. In addition, to remove offices which provide services within the meaning of the Act, premises which come within the definition of retail services but are located above the first three floors are excluded as are barristers' chambers. Leases of 15 years and over which also have obligations to carry out substantial works can also be excluded. This is to remove ground and other types of lease where the tenant has major responsibilities for providing the building and therefore it would be unfair to make landlords responsible for maintaining its structure under the Act..

Immediately the problems with definitions are apparent. VIC has thrown out the blunt instrument of floorspace to attempt to define both retail premises and small tenants. Under the floorspace criteria, large space users (bulky goods for example)

operated by small companies would be excluded while major tenants occupying standard retail premises would be included. Major speciality tenants, such as members of the Just Group, could be included in the Acts in States with the floorspace criteria or a high rent threshold such as QLD, ACT, TAS, NSW and NT and excluded by listing criteria or low occupancy cost threshold in SA, VIC and WA.

The occupancy cost threshold of \$1 million pa in VIC is thought by many interviewees to be very high. In SA it is \$250,000 pa and it was therefore a surprise when the threshold was announced. There was some discussion within interviews of the reasons why the limit was introduced; initial discussions within Government appeared to be in the region of \$350,000 pa to take into account value differences between VIC and SA. One story suggested that analysis of costs suggested that a threshold of \$350,000 included most units in most shopping centres but there would have been a few larger space users which could be on the margin. As the suggested threshold would include most occupiers anyway, the potential for disputes would be removed by upping the limit significantly and in the event only a few more companies would be included under the higher threshold. The major anchors would still be excluded under both the rent threshold and the listing criteria. The evidence of rents set out later in this chapter does give some credence to this story.

The major factor in VIC is therefore listed and unlisted and the use which, as it includes retail services, does encompass a wider definition than the standard retail. The above 3 floors exception excludes some office users selling services but does seem to be a very blunt instrument, at least as blunt as the one it replaces. An alternative approach is the NSW list of users which are specified to come within their Act set out in Appendix Two. Even with the listed and unlisted criteria, a 2005 amendment had to be introduced to deal with listed companies on overseas exchanges.

There is little doubt that the introduction of partial legislation in the UK would introduce the same definitional and operational problems that it has in Australia. Despite nearly 20 years of development and the opportunity within different States to try a variety of different approaches, there seems no definitive view as the best approach. The more simple the instrument, the more blunt it becomes. Floorspace is particularly blunt as it makes no distinction between large and small retail tenants. Small tenants operating large floor plates are excluded while national and international occupiers are included. Rent is less blunt as there is evidence in the UK (Crosby *et al*, 2005) that the small business tenants occupy lower value locations and so there is a correlation between small business and rent. But, as there are problems with the precise measurement of floorspace, there are also problems with the precise measurement of rent and what is to be included and excluded. In addition, the small business competing in the prime market locations in shopping centres is having to pay similar rents to the nationals; in fact, some might argue that the information imbalances would lead to smaller tenants paying higher rents. In the event, the rent threshold in VIC seems to suggest that the small business element of the policy has been reduced to the listed/unlisted criteria. Given the evidence concerning the medium sized business in the UK operating more similarly to larger tenants than smaller ones, this is again perhaps more of a blunt instrument than it appears at first sight. Despite these problems there is no doubt that the legislation in VIC is more

closely policy driven than before and has made a genuine attempt to match policy and operation.

One final question remains. If the policy initiative is small businesses and retail, why doesn't the standard basis of assessing small business, namely number of employees set out in Chapter 3 get utilised in the legislation? This was addressed in DSRD (2001b) and it appears that the reason it was not adopted was for practical reasons. First the number of employees may vary during the lease. Second, the difficulty of verifying the number of employees and the identification of subsidiaries and parent companies for this purpose was cited. Given the difficulties with setting definitive criteria for assessing any of the quantitative indicators (measurement with floorspace and outgoings with rent, which can also change over the lease period), the first reason does not seem so insurmountable and the second reason also appears no more problematic than some of the adopted solutions. It would give the added advantage of being the closest to the policy principle.

4.4 Information and Disclosure

As already indicated, the Victorian legislation requires two elements of information provision; a copy of the proposed lease and the SBC information booklet at the beginning of the negotiations and a disclosure statement before the lease is signed. The provision of the lease and information booklet is controlled by Section 15 of the RLA and states that the landlord or landlord's agent must give them to the tenant as soon as negotiations are entered into. The proposed lease does not have to state the rent, the proposed length of lease or particulars of the tenant. There is a penalty (50 points which currently means \$5,000) for not complying. The copy of the proposed lease must be given at least 7 days before the lease is entered into (Section 17 RLA) and the same rule applies for the disclosure statement in the form prescribed in the regulations. A copy of the Victorian disclosure statement and information booklet is included in Appendices Three and Four.

Section 17 and 18 of the Act are a detailed account of the process and remedies available to the tenant if the copy of the proposed lease and/or the disclosure statement is not supplied. The tenant must give notice that they have not been given a disclosure statement before entering into the premises no sooner than 7 days and no later than 90 days after entering.

If they give notice, the tenant can withhold rent from the date of the notice until the date they receive the disclosure statement. They are not liable to pay rent for that period and can give the landlord notice to terminate up to 7 days after the landlord finally gives them the disclosure statement. If a copy of the proposed lease is not provided or the disclosure statement contains false or misleading information, the tenant can terminate the lease up to 28 days after receiving the late or misleading documents or the date the lease was entered into, whichever happens last. If the tenant gives the landlord a notice of termination, it takes effect 14 days after service but the landlord has the right to appeal against the notice.

There are other provisions concerning information and disclosure appertaining to sub leases and assignments. For the purposes of the policy debate in the UK, this detail is of lesser importance than the effect of these provisions. However, it does indicate that

mandatory provisions can be applied which attempt to enhance the information provision for small tenants at the beginning of the process and prevent surprises after the lease is signed. It also indicates the importance of sanctions for non-compliance.

The RTA 1986 had disclosure provisions but there was no sanction. In addition, the information in a disclosure statement had the possibility of being used in evidence in proceedings for unconscionable conduct under the Trade Practices Act so there was no incentive for the landlord to comply (Croft, 2006b). A tenant was also not likely to terminate just because they had not received the disclosure statement and this was the only sanction in the Act.

In the RTRA 1998, disclosure was given teeth as indicated previously by the introduction of the ability to withhold rent. Croft, (2006b) details the development of the case law surrounding disclosure and whether rent has to be repaid to tenants who have paid rent by mistake not knowing that they can withhold it (the subject of the “Dog Depot” case which commenced in VCAT and was finally decided in the Court of Appeal in February 2006 (*Ovidio Carrideo Nominees Pty Ltd v The Dog Depot Pty Ltd* [2006] VSCA 6)). The tenant’s notice provisions appear to be introduced into the RLA to redress the balance and trying to cap the rent-free problem.

In the previous legislation, the tenant was also obliged to disclose although this was not repeated in the 2003 legislation. The tenant’s disclosure statement took the form of a business plan to be provided 7 days before the lease was signed and it had to be prepared or endorsed by a financial advisor. This process provides a vehicle for making tenants plan their business model with proper advice.

The main issue to arise is whether the information and disclosure provisions work in practice, by informing unaware small business tenants before they enter into leases, and gives them information and opportunity to withdraw from an unfair deal, without heaping unfair compliance costs on landlords. The interviewees, even those acting mainly for landlords, seemed very accepting of the legislation and one interviewee with experience of both UK and Australia speculated that the Australians were less concerned about proprietary rights and more accepting of regulation to curb the excesses of free markets. The vast majority acknowledged the need for it, given the behaviour of shopping centre landlords in the past, and felt that the information and disclosure provisions, plus the sections on lease terms, gave tenants fairer leases. Landlords were forced to identify lease terms and provide full information at the beginning of negotiations and fines were heavy enough to ensure compliance. Draft leases would have to be prepared anyway so the costs were not increased in that respect and, although no work had been undertaken on the awareness of tenants, virtually all interviewees felt that they were more informed and more likely to take advice early in the process. The standard material given to tenants by one institutional landlord seen by the author was extremely weighty and at a Law Institute of Victoria meeting, the consensus was that tenants were frightened by it and therefore did take professional advice. One interviewee felt that the old system of requiring tenants to prepare a business plan was a good idea as it made them more aware of the business risks they were taking when starting a new venture.

However, the same issues of non-representation and low cost representation as in the UK were present. Lawyers felt that they were not able to charge a high enough fee to

small business tenants to undertake the lease scrutiny job to the best of their abilities. Fees for a retail lease of \$80,000 were claimed by one solicitor to be about \$1,200 when \$6,000 would be the proper fee for the proper job.

There were some minority concerns about whether tenant awareness was increased. Because the information is so extensive, some interviewees felt that tenants abdicated all responsibility to professional advisors and took less interest than if the information was shorter and more digestible. One interviewee suggested that telling a prospective small business tenant setting out on their first business venture about all the possible pitfalls of the lease was a bit like telling a bride on her wedding day about the possible messy legal issues that would be raised under any divorce proceedings. Basically they did not want to hear. A number of other lawyer interviewees expressed the same concern that the last thing tenants wanted was any delay to the starting the business and would push for a quick settlement of the process. One interviewee felt that short of running mandatory seminars for all prospective lessees there was not much more than could be done to inform the tenants. The phrase “you can lead a horse to water but can’t make it drink” was mentioned a few times by interviewees.

However, there was also a perceived advantage in that, although large landlords were the headline makers, the behaviour of small landlords warranted as much attention. The benefit of the legislation in general and the information and disclosure requirements in particular was that complex compliance requirements made them also much more likely to obtain professional advice rather than do it themselves.

The disclosure statement was also perceived as a good thing overall. It forced landlords, who had previously hidden some of the more obscure payments which were going to be made under the lease, to disclose them up front and examples such as the payment for the design of the fit out, the inclusion of inappropriate items in service charges and upcoming disruptions to trade are now explicit. However, the right to terminate is not that useful to a tenant who has already sunk a lot of actual and emotional capital into the setting up of the business and it has to be a major issue for the tenant to break the deal at the late stage of the disclosure statement.

4.5 The Role of Small Business Commissioner and Dispute Resolution

The RLA gave significant responsibilities under the Act to the Small Business Commissioner and his office. At present he estimates that around 70% of his workload is related to retail tenancies.

Chapter 6 of the DSRD (2001b) Discussion Paper addressed the introduction of some form of Government sponsored retail tenancy grievance body to hear disputes and a retail leases advisory body to advise on reforms. Chapter 7 discussed the education of stakeholders in the process, particularly new small business tenants and landlords, and noted the role of professional institutions in advising their members.

These issues have basically been rolled together in the office of the SBC. Funded to the tune of \$2 million per annum and with proposals to increase this in the future, the SBC has swiftly obtained a pivotal role in education and information, investigations into unfair conduct and breaches of the RLA, dispute resolution and Government practices as they impact on small business.

The office was inaugurated in the Small Business Commissioner Act 2003 and the role is set out in the Act and reproduced in the 2nd Annual Report of the SBC (2005) covering the year to the end of June 2005. There are 12 specific functions which can be categorised within the 4 functions set out above. The specific functions under the RLA are:

- facilitate the resolution, by mediation, or other forms of alternative dispute resolution, of retail tenancy disputes,
- take proceedings for an offence against RLA,
- endorse a form of standard lease,
- confirm whether a certificate has been given under s21(5) of the RLA,
- prepare and publish an information booklet or guidelines about retail leases that may be purchased on demand by members of the public,
- for the purposes of the Commissioner performing functions under the RLA, create and maintain a register of the information provided under s25.

Section 21(5) of the Act deals with the minimum term of 5 years and if the SBC feels it is appropriate he can issue a certificate varying the minimum term. Section 25 is a requirement to notify the lease to the SBC within 14 days of signing, informing him of the address of the property, landlord and tenant's name and address, the date of signing and other matters as prescribed by regulation. At present these are the lease expiry date and the date of any options plus any email addresses. On a day to day basis the SBC issues certificates under s21(5) enabling a tenant to enter a lease for less than 5 years, deals with disputes and runs the alternative dispute resolution service before it reaches court and appoints specialist retail valuers and quantity surveyors to determine various values and costs under different sections of the Act; for example, a rent determination under a market review. (SBC, 2005).

4.5.1 Information and education

As far as information and education is concerned the SBC has undertaken presentations and small business and industry organisations, a continual regional and suburban programme, involvement at field days, and participation at various conferences. There is an active website. After an initial burst of activity in May 2003, monthly hits on the site settled down to between 2000 and 3000 per month for the first year. In the second year this has risen from about 3500 in May, June and July of 2004 to consistently over 5000 from March to June 2005 (SBC, 2005).

The SBC is already a well-known figure in the property industry. In March 2006, he presented to at least three professional property conferences organised by lawyers and valuers' organisations in Melbourne attended by the author and also presented to the lunchtime meeting of the Law Institute of Victoria Standing Committee on Commercial Leases. The impact of the lease legislation on the industry was also confirmed by the number and attendance figures at these events. The SBC and his

team were interviewed twice for this research and education and awareness is one area that the SBC wishes to particularly increase in the future. The first two years of operation have seen a significant increase in workload from the first to the second year and dealing with the immediate case load and specific functions under the Act have not enabled as many resources to be put into education (SBC, 2005). This may therefore change as the office matures.

4.5.2 Investigations

The second major function is taking action over breaches of the RLA. The RLA has some teeth in that parties can in some circumstances terminate the lease for breaches against the Act and on other occasions there are penalty points awarded. These points translate into monetary fines. The current rate is that each penalty point = \$100 fine. The points and fines are set out in Table 4.1 below.

Table 4.1 – Offences and Penalties under the Victorian Retail Leases Act 2003

Section	Offence	Maximum Penalty Unit	Maximum \$ Value
15	A landlord or person acting on behalf of a landlord, not providing the tenant with a copy of the proposed lease and information brochure	50	5,000
16	A landlord or tenant entering into a lease that is not in writing and signed by all parties	10	1,000
23	A landlord or person acting on behalf of a landlord, seeking or accepting the payment of key money	50	5,000
25	A landlord failing to notify the SBC of the terms of the lease within 14 days	10	1,000
37 (4)	During a rent review, a landlord failing to provide information about other leases in the same building to a valuer upon a valuer's request	50	5,000
38	A specialist retail valuer using or divulging information inappropriately	50	5,000
61 (3)	A tenant failing to provide a disclosure statement and details of information that may affect that disclosure statement, to a prospective assignee	10	1,000
61 (5)(b)	A landlord failing to provide a tenant with a current disclosure statement at the request of a tenant when the tenant assigns the lease	10	1,000
67 (1)	A landlord divulging a tenant's turnover information inappropriately	20	2,000
96 (2)	A licensor failing to provide a disclosure statement and details of information that may affect that disclosure statement, to a proposed licensee	10	1,000
103	During a rent review, a landlord failing to provide information about other leases in the same building to a valuer on a valuer's request	50	5,000
103	A specialist retail valuer using or divulging information inappropriately	50	5,000
121 (2)	A landlord failing to notify the tenant of a land tax assessment within 21 days of receiving that assessment	10	1,000

Source : Brennan (2004)

So far no proceedings have been commenced against any party; however, 112 letters of warning have been sent to individual landlords and tenants. In other cases, assurances about future conduct have been accepted from landlords as the SBC policy is to try and resolve disputes without formal proceedings (SBC, 2005).

However, the annual report of the SBC (2005) does introduce a point of concern about parties not wishing to formalise disputes as they feel that the other party may be able to retaliate in the future. This point was also discussed in a number of interviews where property professionals had found tenants reluctant to take a dispute too far in case the landlord retaliated by refusing to renew at lease expiry. The lack of a right to renew leaves tenants vulnerable to this sort of behaviour. This is because the unconscionable conduct provisions may not protect the tenant as Section 79 of the RLA specifically states that a refusal to renew the lease is not unconscionable conduct.

The highest profile case of breach of the Act concerned the landlord's agents at Preston Market. Information brochures and proposed leases were not provided to some tenants and in approximately 42 instances the leases were not notified to the SBC. These breaches would amount to a substantial fine as each of the information breaches would be worth a \$5,000 fine and the 42 notifications a \$1,000 fine each. However, the landlord's agent agreed to set up a \$20,000 dollar trust fund to help with business counselling sessions for the market tenants.

The notification of leases could form the basis of a retail lease database to inform the market but the Act is definitive that the register of leases is to inform the work of the SBC only. At present this dataset is not being utilised to any great extent and some interviewees expressed some resentment that the additional work involved in notification was not adding anything. One issue discussed at interviews and seminars was the use of the dataset to track the outcome of disputes settled by the SBC dispute resolution mechanism to see if those tenants were treated differently at lease expiry than tenants who had not had a dispute with their landlord. If there were no significant differences, tenants may feel safer raising genuine concerns and letting them run their course within the dispute resolution process.

In contrast to the UK where Investment Property Databank have an extensive databank of leases and the Valuation Office Agency captures and analyses this data for Government business rates (tax) assessments, lease data is not systematically available for any segment of the commercial property market in VIC. It is not collected by the Government and the property industry seems very reluctant to share ideas and data with colleagues in other firms or organisations. Full market analyses of lease length, timing and operation of break options, letting incentives and rent review patterns and type and incidence of lease renewals are rarely undertaken, and even less rarely put into the public domain, and this means that there is little context in which to hold any commercial lease debate. Having said that, the evidence of the case studies set out later in this chapter do show a significant level of conformity within shopping centre leases.

4.5.3 *Dispute resolution*

The objective for the SBC role in dispute resolution is “the timely, low cost resolution of retail lease disputes through facilitated agreement between the parties.” (Brennan, 2006).

A dispute cannot be entered into court (VCAT) unless the dispute has first been referred to the SBC and he has certified that mediation or alternative dispute resolution has not been able to solve the problem. The only exception is an injunction.

Market rent at review disputes are not subject to mediation, the SBC appoints a specialist retail valuer if the parties cannot be persuaded to agree on one themselves. The role in mediation is supervisory and the SBC appoints mediators from a list and at present, the SBC has 90 people either on the list or applying for the list.

Between the inauguration of the SBC in May 2003 and March 2006 over 2000 cases have been referred to the SBC, of which 88% are RLA cases. This has continued to rise with 480 cases between July 2003 and June 2004 and 831 between July 2004 and June 2005, a 73% increase. The SBC offers a preliminary discussion and 28% of cases are settled at this point, suggesting that experienced members of the office are able to discuss the issue and give informed guidance to enable the worried party to see a solution (or to see that they had no chance of getting what they wanted).

Where cases get to mediation it takes place after about 8-10 weeks and takes on average about 3-4 hours. The cost is a set fee of \$95 per party (about £40) but professional representation is obviously at market rates. Mediators are paid \$590 so each one costs the SBC around \$400.

Overall 75% of disputes are settled and they amount to cases worth over \$100 million, with the highest individual case worth over \$900,000. Approximately 25% of cases are brought by landlords and over 60% by tenants. The rest come from other parties; for example, assignees. Where tenants bring cases over 80% are settled. Only 17% of cases by number were about shopping centres and in 34% of these cases it was the landlord bringing the dispute with only 66% from the tenant. This tends to confirm some of the interviewee comments that small landlords were the major problem concerning compliance with the Act, with major landlords having the competence and resources to easily comply with the legislation at little extra cost of compliance. Issues of national conformity have already been seen to be a major concern of larger, national landlords rather than the existence of legislation itself (Cockburn, 2005). Table 4.2 sets out the pattern of cases and resolution in the first 2 years of the SBC operation.

Table 4.2 sets out the results of all disputes concluded prior to July 2005

	2003-04	%	2004-05	%	All	%
Settled prior to mediation	99	26%	175	29%	274	28%
Settled at mediation	168	45%	310	50%	478	48%
Mediation unsuccessful	62	16%	69	11%	131	13%
Not mediated	47	13%	60	10%	107	11%
Total	376	100%	614	100%	990	100%

Source : compiled from SBC (2004, 2005)

The type of issue at dispute has not been analysed by the SBC and the mediations are confidential, but a small sample of cases analysed by the Office of the SBC for this research show a wide range of issues concerning disputes brought by tenants against landlords. They include repairs issues, claims for returns of security deposits, requests to improve or add to premises and to surrender leases or take up options. In the case of landlords it is usually tied to non-payment of rent and breaches of the lease. The types of dispute settled by the low-cost dispute resolution service has not been researched further in this paper but remains an area where further study is warranted if the UK went down the route of a similar Government service. At present, alternative dispute resolution for a range of disputes including landlord and tenant matters is available voluntarily through the RICS Dispute Resolution Service (see www.rics.org.uk/drs) but there is no mandatory provision to use it before more formal processes are initiated.

4.5.4 Effectiveness of the SBC

The interviewees were asked to comment on the effectiveness of the Office of the SBC in achieving its objectives. There was virtually unanimous praise for the present occupant of the Office who was appointed from the beginning. A number of representatives of landlord and professionals who act for landlords suggested that the placing of the lease legislation education, investigation and dispute resolution process in the hands of the Small Business Office was initially treated with concern. The impression was that any small business commissioner would champion the cause of small business without the necessary objectivity to promote certainty and trust from all sides.

The approach from the SBC and his office has to a great extent laid those fears to rest and there is a feeling of even-handedness in dealings so far. In a survey carried out by external consultants for the Government of approximately 300 parties who had used the SBC in one context or another, 81% found the overall process either good or extremely good, 82% found the mediation process good or extremely good, 79% would use it again and 80% said they would recommend others use the SBC.

It does raise the issue of the importance of the appointment, the choice of staff and the choice of mediators, if a low-cost Government sponsored approach is to be adopted. Placing it in the office of the SBC was a risk which some other States have not taken; for example, NSW has a retail tenancy registrar who deals with disputes. The Office of the SBC has a wide remit and operates under a conciliatory approach to investigation and dispute resolution and wishes to expand his educational role to address the awareness issues.

However, one eminent interviewee thought that, although the Small Business Commissioner was doing a very good job on the education and investigation issues, mediation had been around a long time before and all that has happened is that the SBC has taken on an already good system that was operating perfectly well before the SBC took control. It is therefore about the mediation process as much as the vehicle that operates it. This seems to be repudiated by Government who, in their review of 2001 (DSRD, 2001b), blamed the lack of an imposed mediation process on the number of cases going before VCAT relative to what was happening in NSW, where mediation was mandatory. But this ignores the fact that VCAT had the power and used it to refer cases to mediation first and, as indicated earlier in this chapter, also had a success rate of 75%. Both arguments support the mediation process over going directly to court and a majority of interviewees suggested that the informal preliminary channel to the Office of the SBC was a major feature of making small business tenants (and landlords) able to dip their toe in the water and get free, informal, objective advice concerning a possible tenancy issue.

Some of the nationally based interviewees did make comments about the relative merits of the different processes of organisation of mediation in the different States and it was suggested by a very few that the system in NSW did work best. Given the aims and objectives of this research, no attempt was made to delve more deeply into these comments but if a regulated dispute resolution service was initiated in the UK, these questions would need further research as to which facets of which organisation worked best.

4.6 Lease Terms

It is not the intention of this paper to go through the minutiae of the different lease terms detailed in the legislation, rather to identify the major terms and what is considered appropriate and what is not. The major terms include lease length and review, options to renew, outgoings and assignment and subletting.

4.6.1 Lease length and rent review

The minimum lease term for premises that come under the Act is 5 years including any options to renew unless a certificate under Section 21 of the Act is obtained from the SBC and a notice waiving the minimum term is given to the landlord. In the year July 2004 to June 2005, 345 certificates were issued. In the same year 14,430 notifications of leases under the Act were received by the SBC (2005). Exemptions to the minimum term requirement are therefore a very small percentage of all leases which come under the Act, less than 3% of the total. The main reasons for the applications were for tenants to test a new business before committing totally to a long term or they were unsure of their future needs.

Two case studies of shopping centres in VIC illustrate the effect of the legislation on lease terms. Discussions with professionals indicated that these are typical regarding lease lengths in shopping centres.

The first case study is of a regional shopping centre located in the “suburbs” of Melbourne comprising approximately 250 separate tenancies within around 80,000

square metres. The average lease length is 5.5 years however this hides a much more distinctive picture. The average lease length weighted by floorspace is over 15 years and this identifies a major difference between the leases of small and large space users in the centre. The major anchor stores, such as the Myer Department Store and the Safeway supermarket, are offered totally different terms. For example the two major anchors in the case study regional shopping centre both occupy on 20-year terms. There are a number of other less important anchor stores and these are also on 20-year leases. Altogether there are 7 leases of 20 or 25 years but they represent two-thirds of the floorspace. The major anchor store occupies about 25% of the floorspace while another 3 more minor anchor stores occupy a further 25%. One difference between the major and minor anchors is the rent level; the three minor anchors pay about 50% more than the major.

The speciality shops are offered different leases. The normal lease is around 5 years with no renewal rights. Nearly 150 leases were on 5 year terms with another 60 on 6 or 7 year leases. Only 33 leases were for less than 5 years and only 6 leases were more than 7 years but less than 20 years.

The second case study is of a smaller in-town centre in Melbourne. Around 35,000 square metres, the centre has approximately 100 tenants. The two main anchor stores are also on 20-year leases and occupy around 10,000 square metres between them.

The average unweighted lease length is 6.85 years and average lease length weighted by floorspace is 12.8 years. The average lease length weighted by the gross rent payable is less at 9.7 years. The distributions follow a similar pattern to the regional shopping centre although there is more variation. Around 50% of the leases are for 5 years and a further 25% for 6 or 7 years. However, in addition to the three 20 year leases of anchor tenants, there are another 15% of leases which are longer at between 10 and 15 years. These longer leases are offered to the larger space users; for example, two 15 year leases to a single tenant taking a total of 2,250 square metres and a 12 year lease for a 6,500 square metre space user. But a number of the smaller, under 1000 square metre, space users obtained 10 year leases. There is only one lease of less than 5 years.

The rent review type is very consistent with all of the retail unit leases having annual reviews based on either CPI (Consumer Price Index) or fixed increases. Just over 10% were based on CPI and the remainder fixed increases of varying amounts. These ranged from 2% pa to 5% pa. Nearly 60% of these had a 4% pa increase and nearly 20% had a 5% pa increase.

The longer leases had the CPI increases while the shorter leases were on fixed increases. All of the 20 year leases were on CPI and the two 15 year leases on fixed reviews were at the lowest rate of increase at 2% pa. There is a negative correlation (R Squared of -0.4) between the fixed rate of increase and lease length, indicating that in general, the longer the lease the slower the rate of increase. There is one market review in a 12 year lease. This is for the car park.

The interviewees suggested that before the lease legislation was enacted, market reviews with upwards-only provisions were common. As a result of the legislation, which banned upwards-only reviews, the landlords moved swiftly to indexation and

fixed increases. One of the major UK issues is the upwards-only or ratchet clause in the market review. Even within the context of UK longer leases, a ban on upwards-only reviews by the UK government, similar to the ban imposed by Australian lease legislation, may give some impetus to the use of these alternative forms of review; so far little used in the UK.

The rent revision legislation is worded as follows :

Section 35 (1) – If a retail premises lease provides for a review of the rent payable under the lease or under a renewal of the lease, the lease must state –

- (a) when the reviews are to take place; and*
- (b) the basis or formula on which the reviews are to be made.*

Section 35 (2) – The basis or formula on which a rent review is to be made must be one of the following-

- (a) a fixed percentage;*
- (b) an independently published index of prices or wages;*
- (c) a fixed annual amount;*
- (d) the current market rent of the retail premises;*
- (e) a basis or formula prescribed by the regulations*

Section 35 (3) – A provision in a retail premises lease is void to the extent that it purports to preclude, or prevents or enables a person to prevent, the reduction of the rent or to limit the extent to which the rent may be reduced.

Section 35 (4) – However, sub-section (3) does not apply to a provision that uses-

- (a) a basis or formula referred to in sub-section (2)(a), (b) or (c); or*
- (b) a prescribed basis or formula referred to in sub-section (2)(e) that is also prescribed as a basis or formula to which sub-section (3) does not apply.*

Current market rent is defined in Section 37 of the Act and there are also provisions for the assessment of market rent where the review clause is void or does not comply with Section 35 (2) above. Other legislative interference in rents includes the prohibition in Section 23 of premiums for key money or goodwill already discussed in Chapter 3 and the provisions for turnover rents in Sections 33 and 34. Sub-section 33 (4) has twelve specific details of what does and does not constitute turnover and issues include discounts, refunds, tax, fixtures and fittings. A few of the disputes listed previously in the sample of mediation cases were based on these definitions.

Interviewees were asked if there have been any attempts to circumnavigate these and other provisions in the Act and the overwhelming answer was no. The Act appears to have been effective in stopping lawyers inventing any alternative wording which could legally circumnavigate the Act but were in effect an upwards-only review or renewal rent. The market response has been to change the type of review rather than any attempt to maintain the same approach by finding ways around the legislation.

4.6.2 Options to renew

The RLA has provisions concerning the renewal process but as already indicated there is no statutory right to renew the lease although this issue has been the subject of discussion throughout the evolution of the legislation. Redfern (1983) had raised this issue at the beginning of the debate concerning lease legislation and it was again discussed in the DSRD (2001b) review, which called it the “most contentious issue to resolve between landlord and tenant” (DSRD, 2001b, p36). Having identified that 5 year leases with no rights to renew were commonplace in shopping centres, the review paper discussed the issues for and against giving tenants the right to renew and decided that the landlords’ claims that it would stop them being able to change the dynamic of the centre as retailing advanced and changed outweighed the unfair bargaining position arguments of tenants.

The Victorian Government appears to have accepted the data produced by Jebb Holland Dimasi (now Urbis JHD) for the Shopping Centre Council of Australia. This data (reported in DSRD, 2001b) suggested that, from a 10% sample of 423 shopping centre leases, 314 (75%) were renewed by existing tenants. They further suggested that of the 109 not renewed, only 5 leases were not renewed because the rent was too high or the lease conditions onerous. Landlords did not offer 20 tenants new leases, mainly because they had a forthcoming centre redevelopment in prospect, and in 72 cases the tenants decided not to renew their leases. The reasons, according to JHD, were that 9 had gone into liquidation, 48 because of “insufficient store profitability”, 7 retirements or personal reasons and 8 others with reasons not related to the lease. Although the DSRD (2001b) review seemed to place some weight on the JHD assessment that only five retailers had left on account of high rent or onerous lease terms, 75% seems a low retention rate over a fairly short term of five years. The renewal rate of speciality shops cited in the 2006 annual report of Centro Properties for their Australian shopping centres is 83.3%. These centres have a 99.7% occupancy rate.

Many interviewees unfamiliar with UK practice seemed most surprised by two major differences between the UK and Australia. First the right to renew and second the longer leases. In discussion they thought the lack of the right to renew and the shorter leases offered by landlords were compatible in that the lack of income security of the long leases was more than outweighed by the ability to manage the shopping centre dynamically and aggressively. The continual right to renew in the UK was seen as tenant perpetual occupation and gave the landlord no ability to manage the tenant mix and tenant layout. Coupled with the turnover information normally available from tenants by owners, it gives the shopping centre manager the ability to assess individual locations and tenants within the centre, identify non-performing tenants and change them regularly if necessary.

Concerns of interviewees, mirrored in the DSRD (2001b) discussions, were expressed about the misuse of power. They used threats of prospective retailers waiting in the wings and the lack of the right to renew to replace tenants or force them to pay higher rents, which may include part of their goodwill to secure the position. Where the option to renew exists, tenants can, under the RLA, have their rents fixed by specialist valuers, appointed through the SBC, at the market rent as defined previously. But no such rights exist for tenants without the option and the lack of a right to renew is the

most usual scenario in Australian shopping centres for all but the most powerful tenants.

It appears from research undertaken in the US and the UK that landlords can extract higher rents from existing tenants where the right to renew does not exist, the opposite is true where it does exist. Fisher and Lentz (1990) looked at 100 transactions in three US shopping centres and found that, if they took sales into account in their empirical test, renewal rents averaged over 13% higher than new letting rents. If they removed the sales figures from the equation, the differences were over 20%. In the UK, Crosby and Murdoch (2000) analysed UK valuation data in retail, office and industrial markets and found that, in rising markets in the late 1980s, valuers' opinions of provable rents at review or lease renewal, where there were one to one negotiations to fix the rent, lagged their opinions of achievable rents upon competitive new letting by around 10%.

The right to renew therefore appears to be a highly significant financial factor in rent determination and landlords and tenants are therefore going to argue this one for a long time to come, with real rewards available to the winner. In VIC this is the landlord at present. In ACT and SA, the right of first refusal could give the tenant a stronger negotiating position but this research has not examined the outcomes in these States so can make no observations on any differences between them and the rest of Australia. However, it remains an interesting line of research that could be done if the data was either released by landlords or the relevant data was collected on the lease register.

One question that emerges is would the Australian legislation have been needed if the statutory right to renew had been in existence in the early 1980s? Landlords would find it difficult to behave in exactly the same way as they reportedly did if the tenants could not be removed at the end of the short lease. New assignees would have to be given new leases and not held to ransom after a few years or months, having paid significant sums for the business a short time before. However, there would have been nothing to stop alleged abuses concerning service charges. This may explain why the commercial debate in the UK has started from a completely different place; a market crash rather than the development of a particular type of property.

However, it appears that despite a 20 year argument, most States have decided that the statutory right to renew will not be given to tenants so the quality assurance system against the, hopefully, occasional, badly behaved landlord must be policed within the current legislation. As already discussed elsewhere, in VIC the responsibility lies with the SBC.

4.6.3 Outgoings including fit out

Issues dealt with under Part 5 of the Act include the definition of outgoings in Section 29 and issues concerning initial fit out in Sections 30 to 32 of the Act. The part of the Act dealing with the liability for and recovery of outgoings runs to 14 sections, from Section 39 to 52. Other issues include refurbishment and relocation dealt with under Part 6 of the Act. The level of detail of the legislation concerning this kind of lease term is therefore very substantial and reflects in part both the complexity of legislating in this area and its role in the evolution of the legislation. The charges that

landlords applied inappropriate criteria to the allocation and collection of outgoings was set out in the previous chapter and analysis of the case studies and the interview survey responses suggests that some of the issues are still not resolved. As indicated previously, one retailer, who is inside the legislation in some States and outside in others, still has difficulty in getting landlords to be completely open about what is going to be included in the service charge before signing the lease where landlords are not forced to disclose by legislation.

In the regional case study shopping centre, there are significant differences between the service charge payments for the major anchors, minor anchors and the speciality shops. In addition to paying much less rent per square metre than other occupiers, the major anchors also pay a much lower percentage of the service charge per square metre than other occupiers. For example the major anchor store in the regional shopping centre case study occupies 25% of the floorspace but pays only 10% of the service charge. As indicated previously, the lesser anchor stores were also offered long 20-year leases but service charges are not as advantageous as for the main anchors. In respect of three of the minor anchors occupying around another 25% of the floorspace between them, they pay nearly three times the amount per square metre for the service charge than the major anchors. However, the speciality shops fare even worse with a typical amount being double the minor anchors and six times the major anchor when assessed on a price per square metre basis.

The UK policy debate has centred on assignment and subletting, rent review and awareness of small business tenants. Outgoings and their recovery have not been part of the policy debate to any great extent, due in part to the lesser reliance on shopping centres as the mainstay of retail investment and occupation and the low rise nature of commercial office development, creating more single tenancies and less multiple occupation, although it is a major area of dispute between landlord and tenant (RICS, 2006, p1). If similar lease legislation was introduced in the UK, and the legislation looked at all aspects of leasing rather than focus on a few specific issues, then the fit out, repairs, maintenance, refurbishment and dilapidations at the end of leases raise some interesting drafting issues. There is however a separate UK Code of Practice for Service Charges (RICS, 2006) which has addressed many of the issues but, like the Code of Practice for Commercial Leases, it is a voluntary best practice guide, not mandatory.

4.6.4 Assignment and subletting

Part 7 of the Act refers to assignment and termination of retail premises leases and Sections 60 to 64 of the RLA apply. Baddeley (2006) suggests that the actual provisions of the Act set out in those sections do not comprehensively address the issue of assignment but later suggests the parties are probably in much the same position as under the previous Act. However, as concerns sub-letting the position has changed significantly.

Section 60 of the RLA suggests that landlords cannot withhold consent to assignment unless the assignee (a) proposes a use which is not permitted under the user clause; or (b) does not have sufficient financial resources or business experience to meet the obligations of the lease.

The landlord can also withhold consent if the assignor has not complied with reasonable assignment provisions in the lease or, if they are selling their business as a going concern, has not produced their business records for the previous 3 years (or any shorter period that the assignor has carried on their business at the premises).

Issues which arise relate to the minimum term of leases and the disclosure statements. The landlord's disclosure statement must be given to the proposed assignee by the assignor and the assignor must also pass on any details of changes to the information in the statement that the assignor is aware, or should be aware of, since it was given to the original tenant. There is a penalty of 10 points (currently \$1,000) for non-compliance. In order to satisfy the above, the assignor may approach the landlord for a new disclosure statement and the landlord then has 14 days to respond. In the case of an ongoing business the tenant must also provide the assignee and the landlord with a tenant's disclosure statement. If all procedures are operated correctly, the landlord has 28 days to deal with the request. If they do not respond the assignment is deemed to have taken place. In addition, where the business is being sold, the landlord cannot keep the previous tenant, or their guarantors, on any obligations under the lease.

Section 8 of the Act defines the effect of an assignment to be a continuation of the lease, not the granting of a new lease, so the lease expiry date is unchanged. Issues connected with assignees taking the "fag end" of a lease and then not having that renewed are still an issue for uninformed tenants therefore the disclosure provisions are crucial to protecting new tenants in this process.

One of the most surprising aspects of the RLA is sub-letting. Section 63 gives the landlord the absolute right to refuse a sub-letting, licence or concession in respect of all or part of premises. In the RTRA 1998, both assignment and subletting were treated similarly with the landlord not able to withhold consent unreasonably.

One or two of the interviewees expressed their surprise at this hardening of the sub-letting provisions and were unsure where it had come from. The DSRD (2001a; 2001b) issues and discussion papers were silent on sub-letting and did not put it forward as a prospective change. They discussed the nature of an assignment as to whether it constituted a new relationship or a continuation of the existing one. The recommendation was to keep the principle of a continuing relationship with, as indicated above, the disclosure statements being used to inform the new tenant of the issues of taking on this relationship. Sub-letting is not similarly discussed and not mentioned elsewhere in any of the recommendations or in the ORR (2002) Exposure Draft.

The absolute right to refuse sub-letting then appeared in the draft legislation and even a source close to the discussions surrounding the Act did not know where the change originated. The draft legislation was 138 pages long and one interviewee claimed they were given 3 days to comment on the draft; in his opinion hardly enough time to read it let alone notice changes in any detail.

The findings of Crosby *et al* (2005) in the UK were that sub-letting was the primary exit strategy for a number of major tenants, particularly retail who occupy on the longest leases in the UK and have the least incidence of tenant's break clauses in leases. Given the importance of location to retail tenants, the ability to pass on

occupation while still retaining the possibility of claiming back the location in the future is particularly attractive. In the UK, tenants have persuaded the major landlord's institutional body, the British Property Foundation, to ask that their members sustain a voluntary embargo on restricting sub-letting to the contract rent or market rent whichever is higher, a major bone of contention with tenants (BPF, 2005). An Act that allowed landlords the absolute right to refuse would be seen as a major retrograde step to a flexible market. It seems an even more alien concept to an Australian market where landlords have much greater flexibility in moving tenants or refusing them renewals, but are now able to refuse the right to tenants to the same level of flexibility in business. It is therefore, in the context of the Australian leasing market, a very surprising change.

4.7 Conclusions

This chapter has looked at the legislation in one State, Victoria, in more detail to attempt to provide a more in-depth appreciation of the issues involved in developing and framing small business legislation.

The legislation, similar to that in the other States, had its genesis in the perceived behaviour of large shopping centre managers in the 1970s and early 1980s. The case study revealed more detail of what that allegedly bad behaviour actually consisted of and the interviewees gave a consistent set of answers which focussed on the non disclosure of outgoings and other costs and robust policies at lease expiry to maximise short term income. The main policy consideration was therefore to protect small business and try and establish a more equal regime for lease negotiations. There appeared to be no discussion of voluntary codes of practice and the State went straight to legislation.

The latest (2003) piece of legislation appears to be the most policy driven of all with discussion and issues papers preceding the legislation debating what the policy objectives were and how the outcomes might be measured. The policy objectives are clearly stated but performance measures do not really exist, although the SBC has initiated external reviews of the operation of his Office in order to provide some information concerning his major role in the landlord/tenant relationship. The major policy aim is to limit regulation to the minimum to achieve the objectives and the five policy objectives are:

- Government regulation of retail tenancies should focus on addressing information imbalances and the misuse of market power.
- Retail tenancies legislation should only protect small and medium sized retail businesses.
- Government involvement in retail tenancies matters should aim at ensuring that prospective tenants have sufficient knowledge to make an informed business decision.
- While a landlord has a fundamental right of control over the use of its property, this right does not extend to engaging in unfair business practices.

- Landlords and tenants should be able to access a low-cost informal dispute resolution forum prior to any grievances proceeding to formal litigation.

Individual aspects of the legislation are there to deliver these policy objectives and they include the provisions on the role of the SBC, information and disclosure, the scope of the legislation, unconscionable conduct, low-cost mediation and alternative dispute resolution administered by the SBC, and specifying the detail of certain lease terms. Each of these can be related to one or more of the stated policy objectives.

However, in some respects, the discussion regarding leases has been undertaken in a vacuum of information. There is no systematic lease information available, therefore one-off studies of lease terms, lease expiry events and other ad-hoc information dominate the discussions. There appears to have been no survey work of the attitudes and experiences of individual tenants therefore issues of awareness and knowledge are not well understood. In the UK, commercial lease reform has initiated significant research into the operation of the commercial lettings market, using whole market data, and has initiated major developments in existing or new lease databases where that data was insufficient. The Australian debate is undertaken in relative ignorance of data such as lease renewal rates and reasons for renewal and non-renewal, and the actual lease terms for micro, small, medium and large enterprises such as rent, lease length, costs and reviews. What data there is appears to be mainly in the hands of the landlords and their lobby groups. Hence there is only a vague knowledge of whether, for example, medium sized enterprises need protection or not or whether it is only the micro businesses going into leases for the first time that are actually vulnerable. It would appear therefore that the scope of the legislation aimed at small tenants is accepted without too much debate. The register of leases could be expanded into the sort of database necessary to focus the policy debate.

Other issues concerning scope include the concentration on retail. The behaviour of shopping centre managers may have been the catalyst for the legislation but a number of interviewees questioned why only small retail tenants needed the advantages of, for example, information and disclosure. The scope of the legislation appears very narrow, as small tenants of all description are vulnerable to a lack of awareness concerning the implications of the lease. The legislation has moved over the years so that now the definition of the premises and the tenant are wider than retail and include some major business, virtually excluding only those retailers who are listed companies, and including a lot of service providers rather than retailers. A continuation of this movement may ultimately see all commercial premises in Victoria let to unlisted companies at occupancy costs of less than \$1m (or similar depending on price movements through time) included in a Commercial Leases Act rather than a Retail Leases Act. Such a high threshold begs the question of why have partial legislation at all and revert to the UK approach of legislation across all commercial tenancies, the original approach recommended by Redfern (1983) before the original legislation was adopted.

However, while the limitation on small retail exists, the legislation has to identify the limits and Victoria has approached this in a number of ways. Originally, like some other States, it used the 1,000 square metre rule and this has now been thrown out. It had the advantage, subject to a few measurement issues, of being very simple. However, like most simple solutions, it is very blunt. Without some attempt to also

control tenant type, small tenants in large properties are excluded (for example, bulky goods) and small properties let to national chains are included. It is not a piece of small tenant legislation, it is a piece of small property legislation. VIC has therefore rejected this blunt instrument for a more complex set of criteria.

The use of the normal indicator for small business, the number of employees, has been rejected because of changes which might occur during the lease term. Instead it has opted for a combination of rent level and a tenant type indicator. Given that small business does occupy lower value property, it may be slightly more appropriate than floorspace but the occupancy cost level has been set at \$1 million pa, 4 times that in SA. In the regional shopping centre case study used in this chapter, that level of cost only excludes 5 of the 250 leases and those are the main anchor stores. Every speciality shop is included; the highest base rent of any of the speciality shops is \$450,000 pa and that is for a 500 square metre unit. Most are smaller than that. However, if the base rent had been around \$350,000 as was being suggested in some quarters according to interviewees, the \$450,000 pa tenant would be the only speciality shop excluded (although the addition of outgoings may have increased this slightly). Had the limit been the 1,000 square metres they would all have been included. So raising the limit to \$1 million has had virtually no effect and, coupled with the listed/unlisted criteria, is a slightly less blunt instrument than the 1,000 metre rule. The criteria for retail premises is less controversial and attempts to define the included uses, but also keeps open the option of specifying uses that are included by ministerial order. That is the approach taken by, for example, NSW. Given the policy objective, the approach is still very blunt and includes most unlisted companies many of which have multiple outlets and are very experienced tenants. The reasons for not using a tenant size (employees) indicator seem very minor especially due to the short-term nature of the leases.

Information and disclosure are one of the important mechanisms for protecting small tenants and increasing their awareness. Although no research has been undertaken into assessing tenant awareness, the interviewees are virtually unanimous in suggesting that there is little more that can be done to inform tenants outside of a compulsory education programme. The information and disclosure provisions now have teeth and a combination of fines and the ability to terminate the lease for any breach are possible. It appears that no fines have yet been imposed although SBC discussions with some parties who had not adhered to the provisions on information and disclosure have led to financial settlements. The Act is fairly clear on what circumstances require a disclosure statement including assignments. The interviewees expressed some displeasure at the added compliance costs in adhering to information and disclosure provisions. However, overall, the perception is that information persuades tenants who need advice to take it earlier in the deal and disclosure prevents many of the cost issues of the early 1980s happening again. The re-introduction of a tenant's disclosure statement providing a business plan would also impact on the awareness of small business tenants at a wider level than just understanding the implications of signing the lease.

The other area which obtains consistently good comment from interviewees is dispute resolution. Before a case is heard in court, it must have been referred to the SBC for attempted resolution. A conciliation/mediation approach to dispute resolution has been in place for the last 10 years but in 2003 this was placed under the administration

of the SBC who has continued to achieve success rates of around 75% of cases settled either at, or prior to, mediation. Government subsidises the cost so that a mediation fee is only \$95 per party with each party responsible for their own fee.

Only 17% of SBC cases concern large shopping centres and this reinforces the discussion that, although the shopping centre was the catalyst for the legislation, a much wider range of landlords and tenants benefit, or could benefit, from it. A survey of users of the SBC dispute resolution service suggested that they were around 80% satisfied with the process. However, there are issues around the outcome of the disputes in the longer term which have already been discussed above. It is not known if landlords renew leases to tenants who have been in dispute with them during the lease. As the legislation and the SBC are only 3 years old and the minimum lease term is 5 years, this issue is yet to raise its head within the context of the RLA.

Other aspects of the SBC's work also come in for praise from interviewees. His investigations and use of fines has been "light touch" and is endorsed by professional interviewees. The fact that no action has been taken is not seen as weakening the deterrent but, as many of the landlords are also small business, more as part of the education process, his other important role. The SBC would like to see more of his resources pushed to education of businesses about retail tenancy and other matters in the future. He appears to be a prominent figure in the commercial property market. The combined aspects of education and information are seen as the main drivers for a more informed small business market.

The most contentious issue between landlord and tenant in Victoria is thought by Government to be lease renewal rights. At present, there are none although some tenants do negotiate options to renew. Speciality shops in shopping centres rarely get options to renew and the lease term appears to be either 5, 6 or 7 years.

The right to renew has been a feature in all of the reviews of the legislation but so far the government has not followed the UK in giving a statutory right to renew subject to a few grounds for possession or even a right of first refusal, as in SA and ACT. Without the independent data discussed above, it is impossible to evaluate the conflicting claims of landlord and tenant lobby groups. The Government interprets what evidence there is as showing that individual cases of tenants being pushed out against their will are a small minority. The landlord's need to manage the centre effectively has been upheld by the lack of the inclusion of a renewal right or right of first refusal.

The most surprising aspect of the investigation of individual lease terms within the legislation is the position on sub-letting where the 2003 Act introduced an absolute right to refuse. On assignment, the landlord can only resist on a small number of grounds. In previous legislation, assignment and sub-letting were treated similarly. The surprise was the way it emerged from no-where straight into the legislation with no prior discussion, despite an extensive level of consultation on all other aspects included in an issues paper, a discussion paper, an exposure draft and one piece of aborted legislation. This does seem at odds with the process of consultation and the policy objectives of the legislation.

The attempts to stop onerous lease terms being applied appears to be largely successful with the ban on upwards only particularly pertinent in the UK. There does not appear to be any major attempts to draft alternative clauses to get round the Act, it is largely accepted that some kinds of lease term cannot be obtained. The evidence from the case study data does suggest that lease term, rent and outgoings for anchor stores compared to those for speciality shops are significantly different, tending to suggest in a non-information/disclosure regime, abuses were able to be perpetrated on unsuspecting tenants.

This chapter and the one preceding it have broadly outlined the Australian retail leases legislation and added more detail to that framework from one case study State, Victoria. This has enabled some insight to be gained about the policy issues and the practical application of tenancy legislation that attempts to regulate part of a market. On the surface the part of the market referred to are small retail tenants but even defining them is not straightforward. In addition to issues concerning the scope of any legislation, the information and disclosure provisions and the role of the Small Business Commissioners or Lease Registrars are of interest to the UK, regardless of whether it introduces small business tenant or any other kind of legislation. The next chapter concludes this research by assessing the findings from this investigation in the context of the UK Government's desire for more flexible markets in general and to make small business tenants more aware of the implications of signing commercial leases.

Chapter 5 – Conclusions

5.1 Aims and Objectives and Summary of Findings

The aim of the research was to examine perceptions of the effectiveness of small business tenant legislation in Australia and to provide a preliminary evaluation of its potential use in the UK.

The objectives were to:

- Identify the policy aims and objectives of small business tenant legislation.
- Determine the nature and scope of small business tenant legislation in the Australian States in terms of the identification and classification of small business tenants and premises and examine the different strands to the legislation and how they are perceived to impact on the landlord and small business tenant relationship.
- Identify the perceptions of stakeholders in the Australian leasing market and evaluate the perceived effectiveness of the legislation in the context of the policy aims and objectives.
- Discuss the possibility of similar legislation being applied to the UK and provide a preliminary conclusion on the advantages and disadvantages with this option.

The objectives have been addressed by a combination of literature review, analysis of lease terms and an interview survey carried out mainly within a specific case study area, the State of Victoria.

Australia has a federal system of Government with eight individual States and Territories. Lease legislation is the responsibility of the States and despite a number of calls for a uniform tenancy code, the Federal Government has done no more than promote consistency within the States as it has only limited powers in tenancy matters. As a result, eight individual sets of legislation or mandatory codes have developed, although there is evidence of each State being very aware of the developments in other States when drafting amendments or new legislation. There are therefore some common themes within all of the legislation and these have been summarised in compendia published by a number of legal firms including that of Minter Ellison (2006) set out in Appendix One. There have been calls for national legislation from a number of sources including Government reports (Reid and Baird Reports), landlords and tenants but there is no sign or expectation that Federal Government policy will change in the foreseeable future towards a national uniform tenancy code.

There is a consistent view of what drove the legislation in the early 1980s. The development of the shopping centre as the primary real estate vehicle for retail investment and occupation and the consolidation of ownership of major shopping centres in the hands of a few large developers and managers, led to what a number of commentators and interviewees have described as an abuse of power over small business tenants. These abuses concerned issues such as lease renewal, rent and outgoings. It was these concerns that led individual State Governments to legislate concerning retail tenancies in the mid 1980s; firstly in Queensland, Western Australia

and the case study State of Victoria, followed later by all of the others. Codes of Practice were tried in a few States but were either mandatory (closely following the legislation in other States) or voluntary while trying to develop a mandatory code, as in NSW. The consensus in both political commentary and the interview survey was that, in NSW, voluntary intervention was a waste of time as the parties did not conform to the code, even though the code was backed by the organisations acting for both landlords and tenants.

Intervention appears to be taken for granted in Australia and is not seriously questioned. In addition, the scope, policy aims and objectives of the intervention are also not controversial. At present, due to the original catalyst for the intervention, the main policy issue is the protection of small retail business against information imbalances and the abuse of market power. Set out below are the five policy objectives driving intervention in the retail market in Victoria, with the over-riding principle being that legislation should be at the minimum to ensure policy objectives are met.

6. Government regulation of retail tenancies should focus on addressing information imbalances and the misuse of market power.
7. Retail tenancies legislation should only protect small and medium sized retail businesses.
8. Government involvement in retail tenancy matters should aim at ensuring that prospective tenants have sufficient knowledge to make an informed business decision.
9. While a landlord has a fundamental right of control over the use of its property, this right does not extend to engaging in unfair business practices.
10. Landlords and tenants should be able to access a low-cost informal dispute resolution forum prior to any grievances proceeding to formal litigation.

A number of interviewees questioned the retail focus and others did so when questioned specifically on the question of the protection of all small business tenants. The consensus was that the focus on retail was historic and that some of the policy objectives were equally applicable to all commercial and industrial occupiers. The opposite view was expressed in Government discussion papers based upon the location specific nature of retail. They argued that location is particularly unique in retail compared to office and industrial and this is even more so in major shopping centres. This can lead to a sitting tenant issue with an existing lessee particularly vulnerable to being excluded from the location at lease expiry. As other business uses do not suffer with this issue to the same extent this means that it is only retail that requires intervention, given that the policy is to intervene only when absolutely necessary.

There seems to be no evidence, unlike in the UK, concerning the different leases of small, medium and large business and their behaviour when taking new leases. There

is a lack of detailed lease structure and lease events information, which means that policy decisions are taken in a bit of a lease information vacuum. There is the potential to rectify this through compulsory lease registers in the hands of lease commissioners or registrars. Subject to the correct information being collected, issues such as the number of leases renewed, the reasons for non-renewal, comparisons of rents on renewal and new letting and the outcome of lease renewals with tenants subject to prior disputes could all be monitored and generally improve the empirical basis for investigating abuses of the relationship.

The operational difficulties of legislating for a specific part of the market rather than for the whole market are illustrated by the various methods adopted by the various States, with Victoria having recently changed from a floorspace criteria to an occupancy cost based assessment. However, it seems clear that all methods have serious limitations in identifying small business retail tenants. It is interesting to note that no State has adopted the same basis for examining small businesses as that used in national statistics, the number of employees. One reason given by the Victorian Government discussion paper is that this can change over the lease period. The issue has been addressed in Victoria by a combination of value/cost of premises and the nature of tenant, i.e. whether a Stock Exchange listed or unlisted company. This has the advantage of addressing issues of both premises and tenant, as opposed to floorspace or occupancy cost in isolation which purely address premises, but it still remains a very blunt instrument for identifying tenants who come within those needing protection according to the Victorian Government policy aim and objectives.

There are a number of mechanisms for protecting the tenant against misuse of power within the legislation. These include the information and disclosure requirements, the education role of Government including the low cost dispute resolution services and the unconscionable conduct provisions of fair trading legislation in Australia. These are incorporated into virtually all of the States and Territories legislation. Tied up with these issues is the role of commissioners and registrars who are Government appointed to administer some of the processes. In Victoria, the education, investigation and dispute resolution roles are operationalised by a Small Business Commissioner and retail tenancies make up 70% of his workload.

Interviewees perceived that the information and disclosure provisions of the Acts were definite advantages to the unaware retail tenant. Despite the fact that there does not appear to be any other evidence to support this view, it was widely held. At the commencement of negotiations, landlords are obliged in most States to provide an information brochure and a copy of the proposed lease. Even if the tenant does not have the capacity to read and understand the documentation, lawyers in particular are convinced that it persuades tenants to get professional advice earlier, and therefore parts of the commercial deal are discussed before the lease is close to signing. Later on in the process tenants have invested more time in the planning of the business and do not want lease issues to disturb the whole project so it is important for the advice to come early in the process. Interviewees cited cases of tenants ignoring advice not to take a lease without changes to particular terms.

Other advantages of information and disclosure, coupled with the detailed provisions on lease terms, included stopping landlords putting together particularly onerous leases. Some larger landlords have produced standard terms, which had to comply

with the legislation. Unfair recovery of outgoings, or unfair provisions regarding other costs, are therefore harder to apply under the legislation. Although often these standard leases are used regardless of whether tenants are inside or outside of the legislation, it has been claimed that larger more powerful tenants find it harder to get full disclosure before signing leases when they are outside the legislation

There are a range of penalties for non-compliance with information and disclosure provisions and this has given tenants some redress after signing a lease if an unfair provision comes to light in late disclosure. Other penalties for non-compliance with the legislation also act as a deterrent to any attempt to avoid certain aspects of the Acts. Avoidance does not seem to be a problem. The interviewees and the statistics of the Victorian Small Business Commissioner show that very few investigations have been necessary. Those that have are more about ignorance rather than any attempt to avoid the legislation. This tends to confirm interviewee opinion that the legislation is largely accepted as an irritant rather than a major institutional blight on the market. Compliance costs are higher but not so much so that it stifles development and investment, and fairer leases result.

Tenant disclosure is present in a few States and can consist only of a declaration that the landlord has complied with information and disclosure provisions. However, it can include disclosure in the form of a business plan which has the affect of ensuring that a tenant has planned any venture properly and has formed plans in conjunction with external legal, financial and/or business advisors. This vehicle for attempting to increase the wider awareness of the tenant has been dropped in the most recent Victorian legislation.

Low-cost dispute resolution by mediation or other means, before the case is allowed to go before the courts, is a feature of much of the legislation. In Victoria it is organised through the SBC who has a 75% success rate in settling disputes by informal discussion prior to mediation or at the formal mediation. Interviewees were virtually unanimous concerning the efficiency and effectiveness of this mechanism and advantages included giving small business tenants a place for informal objective advice as well as the good rate of settlement. There were concerns from landlords in Victoria about giving jurisdiction over the mediation process to a small Business Commissioner, who might have a small business tenant “agenda”, but the perceived objectivity in the way in which the present incumbent operates has silenced these concerns.

The retail lease legislation in Australia prescribes what is allowed and what is not allowed across many individual terms of the lease. Rent determination at review, the type of review, including banning any attempt to install an upwards-only review, issues on assignment and sub-letting and repairs and outgoings are all dealt with in the legislation in detail. The introduction of the absolute right for landlords to refuse sub-letting in Victoria was a surprise to many interviewees but they perceived most prescribed lease clauses to be fair and reasonable and there seemed to be little attempt to circumnavigate them. The banning of market upwards-only reviews did lead to a reduction in market reviews and the use of indexation and fixed increases. The minimum term is 5 years under virtually all the legislation and speciality shops only get that term with no right to renew. The major and minor anchor stores are offered much longer leases (10/15/20 years) and rights to renew.

There is no statutory right to renew in Australian legislation although SA and ACT have a relatively weak right of first refusal (with landlords able to claim significant grounds to refuse in ACT). Renewal rights have been debated throughout the period of the legislation and so far landlords have managed to persuade Government that it would stifle the flexibility to adapt centres to changing retail formats. The arguments of tenants are that individual retailers are quite capable of adapting to change and need the protection of the right to renewal to equalise the information imbalances and stop abuses of market power. This research has not examined these issues as they are outside the aims and objectives but there is no doubt that it is a fundamental lease issue, with evidence that the level of renewal rents is significantly affected by the lack of or presence of a right to renew.

In the event that the current draft of legislation in WA is enacted, unconscionable conduct will be included in the retail lease legislation in every part of Australia. There are serious doubts of the ability of tenants to bring a successful case of unconscionable conduct against a landlord for all but the most malevolent of behaviour. Despite this, the interviewees were of the opinion that this was a far greater deterrent than being cited for not complying with a particular item within the Act (such as failing to provide information at the commencement of negotiations). Although the unconscionable conduct issue has not been fully developed in this research, in principle it remains an interesting discussion point for the UK policy debate on commercial leases, but has far wider implications for business contracts in general.

5.2 Policy Implications for the UK

This research has the objective of informing the current UK policy debate on commercial leases. At present the UK Government have three main issues following a debate that has spanned 14 years since 1992. The general policy agenda is bringing flexibility and choice to the commercial leasing market. These individual issues include flexibility in sub-letting, the use of upwards-only rent review clauses in longer leases and the awareness of small business tenants. Research into small business tenants in the UK has found that very small tenants approach the process of taking a lease differently to medium and larger sized tenants. They are more likely never to have taken a lease before, to take the first lease on offer, not to negotiate and not to take professional advice. If they do take professional advice, they take it after the commercial side of the deal has been reached between them and the landlord. The size of the deal does not warrant a high enough fee to enable all but the most conscientious lawyer to do a detailed reading and negotiation of the proposed lease, some of which run to tens of pages. By this stage the tenants are keen to take up occupation and almost resent any delay caused by a conscientious solicitor renegotiating onerous clauses.

Part of the Australian policy objective is to inform and educate so that small businesses make more informed decisions. Interviewees suggested that, in their experience, Australian small business tenants behaved similarly to the UK and fees were also not likely to be high enough to fund a fully professional job on the lease terms. Therefore the Australian legislation is aimed at similar issues to the UK.

The first policy issue for the UK is the scope of any protection. In Australia, it is generally accepted by most commentators and interviewees that it is a small retail business issue. In the UK it is an issue across all commercial markets. The retail physical structure does appear to be a bit different in the UK, although out of town shopping centres do exhibit similar characteristics to Australian shopping centres situated in suburban areas. However, in retail there is an added emphasis on well-located strip shopping in the UK and this lessens the location specific issue that drives the legislation.

Despite the fact that much of the political pressure in the UK has come from retail tenants, the study of Australia does not indicate that the UK policy objective should shift towards retail; in fact, this study probably raises more questions for the Australian legislation regarding its narrow focus on retail. There is no doubt that this is being challenged in certain quarters and within the legislation itself. In some States some commercial offices are included and, in Victoria, retail services are also included, so there is already a movement away from retail. Given that the information and education provisions could relate to all uninformed small business tenants, it is only the likelihood of a misuse of market power in specific locations that distinguishes retail from others.

The actual problems with legislating on part of a market are fully illustrated with the attempts to define the premises and tenants which come under the Act. Most States use the premises as the basis of inclusion, not the tenant. This leads to huge anomalies with small businesses taking large areas outside the Act and large businesses taking small areas within the Act. Attempts to use tenant type have ignored the normal indicators of small business, number of employees and turnover, and used listing on stock exchanges or lists of uses. The differences between the very small (micro) tenant and small and medium sized tenants are not identified. A floorspace indicator appears inappropriate for retail and if the intention were to incorporate all small business tenants then it is even more inappropriate. An occupancy cost indicator has some merit but in Victoria it is set so high that it virtually includes all but the major tenants. Listing also has some merit but again includes many tenants who do not suffer from lack of awareness. As it is a tenant type issue, the over-riding principle should be to base it primarily on the tenant rather than the premises and keep it simple (which means based on fact at a particular date). This tends to lean towards a basis of number of employees at the date of the lease, perhaps backed up by a rent indicator.

The above discussion on defining tenants and premises inside the Act raises a more important policy issue. Although the Australian legislation was originally aimed at small retail tenants, the criteria include many larger organisations. In the UK, research has shown that it is the very small tenant who behaves differently but in Australia the legislative distinction now appears to be between the very large tenants and the rest. The large listed companies operating as anchor stores taking large spaces appear to be excluded from the Acts but often national chains are included. This appears to raise the question of whether legislation should be aimed at small tenants; in many States in Australia it has ceased to be small tenants only and it would be a very small step to include all tenants. This would then bring Australia into line with the UK where differential legislation is not yet on the agenda. However, if the main policy objectives are to stop the abuse of market power and inform small

business, then legislation should be aimed at those who need protection. Both Australia and the UK seem to have lost their way somewhat in matching the intervention to the policy aims and objectives.

One other operational issue was raised in the interviews and that is the creation of a two-tier market, with landlords much more willing to let to tenants outside the Act rather than inside due to added compliance costs. However, there is no evidence of that in Australia (from the interviewees who were asked that specific question) and it is likely that any discrimination on that account is already present in the UK, given the importance of covenant strength to the value of investment property. However, these responses may be distorted by the fact that the two-tier market does not really exist in some States.

Education and information are two important initiatives in informing tenants and the use of information brochures is universal in Australia at the commencement of the lease. There is at very least a perception that it has a positive effect on the awareness of tenants and that they take professional advice earlier. The contrast between the UK and the Australian leasing process is probably most observable in this respect. In the UK it was found that initial information was usually the rent plus other terms by negotiation. The unaware tenant then went on to agree a short set of heads of terms, often on less than one side of paper, before instructing a solicitor (although it was found that heads of terms were getting more detailed for larger, better located properties) (Crosby *et al*, 2005). In order to inform tenants at the beginning of negotiations, the UK Government hoped that landlords and their agents would provide copies of the voluntary Code of Practice to tenants but this was found to happen only occasionally and was certainly far from universal. In the UK tenants' survey only 18% of small business tenants who had recently negotiated a new lease were aware of the Code of Practice (Crosby *et al*, 2005).

The failure of landlords and professionals in the UK to disseminate the Code of Practice, despite some improvement in the situation between the first and second code, and the success of the Australian approach raises the question of a more regulated approach in the UK. The Victorian legislation imposes fines for non-compliance and gives termination rights to tenants. In the UK, the Code of Practice could act as the information brochure and it would not be onerous to ask landlords to have a draft copy of a lease drawn up before putting the property on the market

If the government is serious about the awareness of small business tenants then the same goes for disclosure statements and notification of leases. Notification could be limited to certificates of compliance, although the advantages of having basic lease information for policy discussions should not be underestimated. Disclosure provisions could be by both landlords and tenants with tenants confirming receipt of the statement. A business plan would also be compatible with the Government's desire for a more informed business community although that raises questions of why only include business tenants, and not all businesses, in compulsory business plans.

On the same theme of education, the role of the lease registrars and commissioners has generated significant approval ratings from the interviewees in Australia. Despite some arguments about the best system, a focus for education, investigation and alternative dispute resolution, giving a one-stop shop for all commercial tenancy

matters, has some merit. The comparison with the UK Small Business Service website (www.sbs.gov.uk) and the Victorian Small Business Commissioner website (www.sbc.vic.gov.au) is very stark with virtually no property matters highlighted in the UK. Mediation of disputes, regardless of the administrative arrangements, received universal praise, with the dispute being about which system was the best, not about the overall concept of low-cost mediation and alternative dispute resolution.

The aspects of information, disclosure, mediation and the introduction of lease registrars/commissioners have been well received in Australia and could be addressed in the UK in isolation from the issues of legislation across the whole market or part of a market. They could also be isolated from the discussion of individual lease terms. However, there is a certain irony in the fact that sub-letting rises to the top of the lease clause flexibility debate in the UK at a similar time to when it gets made more difficult for tenants to sublet in Victoria.

There is one aspect of lease terms that is very interesting for the UK. Obviously there are significant differences between the lease structures in the UK and Australia, not least the length of leases, but when upwards-only reviews were banned by legislation, interviewees operating at the time of the ban suggested that market reviews in leases disappeared very quickly, to be replaced with fixed increases or indexation. There has been some comment about a similar move in the UK if they were banned there although there is a different scenario between a fixed increase or an index linked increase in a long lease of over 5 years than for a short lease of 5 years or less.

Finally, a wider issue than small business tenancies is the fair trading legislation incorporated into retail leases legislation in Australia. It has not been possible in this research to do more than scratch the surface of this issue so no conclusions are made concerning this aspect. However, it is apparent from the interviews that landlords attach some importance to it and they are aware of the effect on brand image of a determination concerning unconscionable conduct.

Overall, there are significant differences between Australian leasing practices and the UK but these have been isolated to put the differences processes examined in this research into context. Despite these differences, both jurisdictions appear to have similar if not identical issues concerning the education and protection of tenants. In Australia the emphasis is on retail and this research questions whether that is a sustainable policy position for the Australians. However, as a result of their retail issues in the 1980s, they have developed legislation that goes far beyond the UK apart from one major respect, the statutory right to renew. Although there might be some suggestion that the attempt to isolate parts of the market has caused major operational difficulties, and some might suggest that the hundreds of pages of legislation is a sledgehammer to crack a nut, the information, disclosure, unconscionable conduct and dispute resolution provisions, and the Government input into administering these provisions, could be the basis of solving at least one of the UK's major commercial lease policy issues, the awareness of small business tenants.

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