Draft Retirement Villages Regulation 2009 and Regulatory Impact Statement

Submission of the Urban Development Institute of Australia NSW

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Introduction

The urban development industry is a major contributor to the NSW economy and its investment decisions are guided by key strategic documents including the State Plan, the Sydney Metropolitan Strategy and various Regional Strategies. The residential sector of the industry alone, including retirement living, contributes more than $15 billion worth of activity to the NSW economy annually.

The Urban Development Institute of Australia NSW (UDIA NSW) represents the leading participants in the urban development industry with over 550 member companies. This includes developers, operators, and industry practitioners in the retirement living sector. UDIA NSW believes in sustainable development including the preservation of environmental outcomes in balance with social equity and economic stability.

This submission has been prepared by the UDIA NSW Seniors Living Committee, in response to the *Regulatory Impact Statement* (RIS) issued in relation to the *Retirement Villages Regulation 2009* (the Regulations) promulgated under the *Retirement Villages Act* 1999 (the RV Act). It is noted that the proposed Regulations completely replace the existing Regulations under the RV Act.

The Regulations seek to introduce a number of new provisions which are summarised under section 7 of the RIS and this submission responds primarily to those new issues. As a general statement, the majority of the Regulations do not give rise to matters that UDIA NSW would consider inhibit the development of a viable retirement village sector.

For the most part, the Regulations are restatements of the existing Regulations with amendments to capture aspects that have developed as industry practice has evolved over time. This submission does however identify key aspects of the Regulations that require further clarification in order to ensure certainty for developers, operators and residents alike.

The primary areas of concern to UDIA NSW, and the matters for which this submission is directed towards, relate to:

- capital maintenance;
- matters that may be funded by recurrent charges;
- payroll tax and head office expenses;
- contingencies; and
- the definition of 'resident'

UDIA NSW submits that these items will significantly impact existing retirement village operators as they will impose greater ongoing maintenance costs that are not recoverable against residents. These increased costs will be imposed in circumstances where the operators cannot make any adjustment to the ingoing contribution or deferred management fee to defray the added costs. The increased costs relate to external painting, maintenance of capital items and head office expenses.

In so far as the Regulations affect future retirement living developments, they will force operators to weigh up alternative methods of charging deferred management fees and ingoing contributions to recover the increased costs of operation. As a result, when faced with provisions that financially impact existing operators and residents alike in the manner proposed by the Regulations, there is an increased likelihood of disputes. This will lead to a need to seek judicial clarification which may not always reflect the intention of the legislation.

Effect on industry

The Regulations and the below recommendations must be viewed in the context of the objects of the RV Act which, following the most recent amendments to the Act, include an object to: *'Encourage the Retirement Village industry to adopt best practice management standards.'*

Capital maintenance

The relevant regulation is contained in Clause 4: The matter sought to be addressed by the draft regulations is to reduce the number of disputes relating to what constitutes capital maintenance.

The majority of Tribunal decisions issued by the Consumer Trader and Tenancy Tribunal relate to matters of determining what items of work undertaken at a village constitute maintenance or replacement. This regulation seeks to reduce the incidence or opportunity for operators to continually seek to repair items beyond the economic life in instances where it would be cheaper and more practical to replace such items.

The effect and operation of the draft regulation must be viewed in the context of the current amendments to the RV Act.

1. Sections 92, 93 and 97 make it clear that the operator is to maintain each item of capital for which the operator is responsible and through the structures of Division 2 Part 7, may utilise the capital works fund to fund such maintenance.

2. Section 97 of the Act makes it clear that the operator of the Village must bear the cost of capital replacement in respect of an item of capital for which the operator is responsible.

The effect of clause 4 of the draft Regulations is to extend and limit the definition of *'capital maintenance'*. The extension of the definition in clause 4(1) goes to:

(a) painting of internal surfaces of internal services – 4(1)(a)(i);

(b) maintenance or replacement of furniture and other *'non fixed items in common and kitchen areas'* – 4(1)(a)(ii);

(c) maintenance or replacement of window coverings in common areas - 4(1)(a)(iii);

(d) replacement of a component of an item of capital but only if the component is replaced in the course of maintaining the item and the cost of replacing the component is no more than 10% of the cost of replacing the whole item - 4(1)(a)(iv).

3. Clause 4(1)(b) then prescribes a number of things as *not* being capital maintenance, being:

(a) painting external surfaces - 4(1)(b)(i);

(b) repair of an item of capital if that item has already been repaired twice within a period of 12 months before the proposed repair - 4(1)(b)(ii);

(c) work that is required by law to be carried out such as complying with fire safety regulations - 4(1)(b)(iii);

(d) work on vacant residential premises - 4(1)(b)(iv);

(e) maintenance of an item of capital (including the replacement of a component of that item) but only if the cost and maintenance is more than 50% of the cost of replacement of the whole item - 4(1)(b)(v);

(f) maintenance of an item of capital that is carried out for the purpose of enhancement or improvement of the item or the retirement village in which the item is located or that results in enhancement or improvement to the item or Village - 4(1)(b)(vi).

UDIA NSW contends that instead of assisting and removing the argument as to what constitutes maintenance or replacement, the extended definition of capital maintenance further compounds the disputes already being brought before the Tribunal. It also potentially causes financial detriment to residents through increased maintenance charges, by creating a bias towards replacement of capital items, rather than improved maintenance practices.

Regulation 4 must also be read with Regulation 5 which further defines what is 'an item of capital' and in turn refers to fixtures, fittings, furnishings and non-fixed items. The structure of the two regulations means that there is scope for continued argument as to the following issues:

(g) what is *'fixed'* and *'non-fixed'* items? – This is a question of fact and degree which is often argued in income tax matters.

(h) do *'window coverings'* include blinds and curtains?

(i) does *'10% of the cost of replacing the whole item'* require an ongoing valuation of items of capital in the Village? If this is correct, it will invariably lead to increased costs to residents as operators will need to undergo regular surveys of the value of their capital items. It may also delay necessary repair work so that the costs of maintenance fall within a particular level.

(j) what is meant by the expression *'item has already been repaired twice within a period of 12 months before the proposed repair"*? That is, is it referring to a single component in an item of capital, or to the item of capita itself? The expression is ambiguous and will cause confusion for residents and operators alike.

(k) what is meant by *"work required by law'.* This is not able to be properly defined. The provision is meaningless as there is no guidance as to what is meant by 'required by law'. The expression could literally apply to all maintenance as parties to a contract are 'required by law' to comply with their obligations. Similarly, duties of care such as are owed by an operator to a resident are 'required by law'. All matters relating to occupational health and safety, environmental and workplace are 'required by law'.

(l) the maintenance costs of more than *'50% of the cost of replacing the whole item'* gives rise to the same problems as assessing the component cost of an item of capital. This gives rise to issues of valuing each item of equipment;

(m) maintaining items of capital carried out for *'the purpose of enhancement or improvement of the item'.* This element of the Regulation gives rise to a subjective assessment of what is enhancement or improvement as distinct from merely repairing and maintaining an item or restoring an item to working order or good repair which is the exception contained within Regulation 4(2).

RECOMMENDATION 1

UDIA NSW recommends that in order to protect against the mischief of operators extending the economic life of items of capital, and in order to protect the structure of the Regulations currently drafted and minimise drafting requirements, the following amendments to the draft Regulations be adopted:

- *delete 4(1)(b)(vi) and 4(2) – this is so as to avoid the subjective issue of what constitutes 'enhancement' or 'improvement';*

- *delete 4(1)(b)(i) painting external surfaces – this is an item of capital maintenance and gives rise to the argument as to what constitutes external. Tribunal decisions have supported the position that painting is a proper form of capital maintenance and there appears to be no good reason why painting generally should not be so protected. There appear to be arguments as to the enhancement of the property to the benefit of the operator however such arguments ignore the benefit to residents in having their environment maintained and their ongoing sharing in a capital gain. It is the mutual benefit of residents and operators that such work be undertaken on a regular basis as part of the ongoing maintenance of the village.*

- *delete 4(1)(b)(ii) – repairing an item twice – this definition is ambiguous and will give rise to significant debate with residents. There appears no basis upon which an item of capital as distinct from a component can be identified. Perhaps the issue should refer to a component of an item of capital;*

- *delete 4(1)(a)(iv) – it is highly subjective to discuss repairs in terms of 'a component'. It may be useful for large items of capital but what happens in the case of smaller items such as taps and bathroom fittings? To put an arbitrary figure of 10% of the cost of replacing a component item does not assist the determination. It also gives rise to the bias towards replacing an item of capital. For example if a bus costs $40,000 and the replacement of a gear box is $5,000, the replacement of the bus and the capital works fund would be permitted but the replacement or maintenance of the gear box would mean that the item of maintenance would fall outside of capital maintenance.*

These amendments would then leave a situation of defining things which are not capital maintenance to be:

- where maintenance costs exceed 50% of the cost of replacement; and

- work on vacant premises.

Matters funded by recurrent charges

The matters for consideration upon review are:

1. Regulation 17(2).

2. Regulation 26.

These regulations give rise to matters that are contained within the proposed annual budget and for which expenditure may not be financed by way of recurrent charges. In relation to Regulation 17(2) the standard set is to show *'the actual goods and services to which (any administration or management fee) relate'* and *'the cost of each of those goods or services'*.

The provision requires a direct connection between the goods and services and the cost of goods and services in the context of administration of management fees. The difficulty is that work undertaken by organisations that operate across numerous Villages will have resources which provide goods and services that would obviously provide benefit (eg a state coordinator for external activities at villages) to all Villages.

However, without some study undertaken of the work done at head office, which itself will give rise to increased costs to operators, an operator would be unable to establish the *'actual'* goods and services and the *'cost of each'* of those goods and services. It is submitted that Regulation 17(g) cures any mischief that the Regulations are seeking to avoid in regards to costs not associated with the operation of retirement village being passed to residents in the Village.

Regulation 17(g) works efficiently to ensure that costs relating to the operation of the Village are passed to Villages in a transparent and equitable manner. This was made apparent in the matter of *Australian Retirement Homes Pty Limited v Residents Committee of Minkara Retirement Village* (May 2009), Commercial Trader and Tenancy Tribunal.

Similarly, Regulation 26(e) seeks to also raise the costs associated with the operator's head office, being costs that do not directly arise from the operation of a village unless the costs are directly associated with providing services to residents of the retirement village. Again, this provision seeks to identify the direct relationship, when in the circumstances, Regulation 17(g) does the work in an efficient manner.

Following from that, clause 26(f), being any flat management or administration fee not to be financed by way of a recurrent charge, becomes superfluous.

RECOMMENDATION 2

UDIA NSW recommends the following changes should occur to the draft Regulation:

1. *Regulation 17(2) – delete the words 'actual' before the words 'goods and services to which they relate' and delete all of the words 'and the cost of each of those goods or services'. These changes will allow that it is necessary for the annual budget to include administration and management fees to be broken down to show the goods and services to which they relate. That way, it can identify the nature of the goods and services being the application of personnel or resources to Villages as distinct from seeking to identify the direct nexus.*

2. *Regulation 26(e) and (f) – delete '26(f)' and amend '(e)' by deleting the word 'directly' before the words 'arising from the operation' and delete the word 'directly' before the word 'associated with providing services'. This way, it meets consistently with the provision of 17(g) to show where the expenditure arises.*

Payroll tax and head office expenses

This part relates to Regulation 26(d) which seeks to deny payroll tax being funded by way of recurrent charges. This arises from the decision in *Australian Retirement Homes Pty Limited v Residents Committee of Minkara Retirement Village* which is referred to in the RIS.

What is missing from the analysis in the RIS is that it was not necessarily the item of expenditure, being payroll tax, which was the subject of the decision. An analysis of the decision shows that the Tribunal applied Regulation 19(g) under the existing regulations which is in the same terms as Regulation 17(g) to show that if an item of expenditure relates to the operation of one or more Villages, then so long as the expenditure can be explained across those Villages and shown to be apportioned in a transparent manner, the expenditure can be passed to residents.

Payroll tax is an expense related to salaries and wages. Salaries and wages are in turn directly related to the services provided by residents. UDIA NSW contends that there is no reason in principle why payroll tax should not be charged to residents in a retirement village similar to salaries or wages.

RECOMMENDATION 3

UDIA NSW recommends that Regulation 26(d) be deleted.

Definition of resident

Regulation 8(6) extends the definition of a resident to include spouse or a de facto relationship with another resident, and then seeks to exclude from the operation of that resident, the effect of a resident's will. It appears the purpose of the regulation is to protect the current occupant of a retirement village premises from being removed or asked to leave upon the termination of the lease by the named resident. The difficulty with the regulation is however, that it requires:

1. the resident or the operator to ascertain whether another person living in the premises at the time of the person's departure (Regulation 8(1)(b) *'occupies residential premises in the retirement village with that resident'*) which is a question of fact, that of all people the operator is not able to properly characterise; and

2. seeks to remove the entitlement of that occupant once the operator has determined the operation of the resident's will (Regulation 8 (2)).

Regulation 8(2) seeks to exclude the operation of 8(1) *'if the terms of the other resident's will are such as to require (whether directly or indirectly) the person to vacate the residential premises concerned.'*

It is highly unlikely that any will would state categorically that any occupant of a retirement village premises must vacate after the named person dies. It is likely a deceased's last will and testament will state that all assets are to be collected by an executor and disbursed to named beneficiaries in a particular way.

Such a provision in a will would ordinarily mean that the retirement village premises need to be *'sold'*. However, the current occupant of the premises under a de facto relationship could frustrate the operation of a will under this Regulation and therefore prolong estate matters.

Further, the regulation seeks to have an operator determine the operation of a will before any grant of probate is issued. Regulation 8 does not refer to any point of a grant of probate or letters of administration. It is submitted that it puts an operator of any nature in an impossible position of ascertaining the entitlements of an estate upon a resident vacating premises, and the rights of another person occupying the premises who is not named on the retirement village contract.

It is further submitted that the appropriate course is that only a named resident be permitted occupancy and if a spouse or de facto were to join those premises that there be a method of either notation or that they specifically be joined as a party to the contract which consent the operator may not unreasonably withhold.

RECOMMENDATION 4

UDIA NSW recommends that either:

1. *Regulation 8 be deleted in its entirety; or*

2. *Regulation 8 be amended so that the resident is obliged to notify or seek the addition of a spouse or de facto as a 'resident' under a 'resident's contract' for the purpose of the RV Act with such consent not to be unreasonably withheld by an operator for those persons to obtain the benefit of occupancy.*

Conclusion

UDIA NSW appreciates the opportunity to provide input into the draft Regulations. As the peak industry body representing the interests of the urban development industry in NSW, UDIA NSW believes it can provide credible and balanced input into the development of the final Regulations.

UDIA NSW is pleased to assist Fair Trading in the development of Regulations that will have an impact on the retirement living sector and elaborate on each of the recommendations discussed above. This Submission has been developed with the generous assistance of leading industry practitioners on the UDIA NSW Seniors Living Committee.