



Never Stand Still

Built Environment

City Futures Research Centre

Improving housing security through residential tenancies law reform

Submission to NSW Fair Trading

Dr Chris Martin

January 2017



UNSW
AUSTRALIA



Introduction

This submission is about improving the housing security of tenants through tenancy law reform, and particularly about the question of whether long fixed term agreements can be used to this end.

The submission begins with a discussion of what ‘security’ means in the context of the Australian private rental sector. In light of this discussion, we submit that law reform focused on long fixed terms is not the best way to achieve improved security for tenants. Long fixed terms, as they are currently conceived of at law, are not useful for landlords or tenants in the Australian private rental sector, and trying legislatively to make them more useful by altering other legal rights and liabilities is difficult and risky. The result may be a regime in which long fixed terms remain unused by most parties, but used in some cases to the disadvantage of vulnerable tenants.

Fixed terms are just not a good starting point for pursuing the objective of greater security for tenants. A better approach would be to amend the prescribed grounds and notice periods for termination and rent increases by landlords.

Security, mobility and autonomy

The Australian Bureau of Statistics’ 2013-14 survey of Housing Mobility and Conditions reports that the large majority (81 per cent) of households living in private rental housing have lived in their current premises for less than five years, and 70 per cent of private renters who had moved in the past five years did so from another private rental dwelling.¹ About half of households who had moved from a private rental home did so mainly for ‘personal reasons’, including ‘family reasons’ (25 per cent), ‘employment reasons’ (15 per cent) and ‘lifestyle change’ (seven per cent); another 18 per cent moved to get a bigger or better home, and two per cent moved in order to downsize. The figures imply that about 15 per cent moved because they had been given a notice of termination by the landlord.² In a 2015 survey of private renters conducted by City Futures and other researchers, 25 per cent of tenants had made their previous move at the instigation of the landlord; also, looking forward, 25 per cent said that they were not confident in being able to remain in their current premises.³ In a 2014 survey of renters by the Tenants’ Union of NSW, 14 per cent said they had made their previous move because of a termination notice from the landlord; but 92 per cent said they worried that, if they had to move, they would not find suitable, affordable housing, and 77 per cent said they had put up with a problem in a tenancy, or declined to assert their tenancy rights, because they were worried about adverse consequences.⁴

¹ ABS (2015) *Housing Mobility and Conditions, 2013-14*, cat no 41300DO004.

² The report of the 2013-14 survey omits the figure for private renter households whose main reason for moving for notice from the landlord. However, figures for most other categories of reasons are given, and when inapplicable or negligible categories are excluded, the 15 per cent figure is implied. This is roughly consistent with the report of the 2007-08 survey, which gives the figure as 15.8 per cent.

³ Pawson, H, Hulse, K and Morris, A (2015) ‘The rise of long-term private renting in a home owning society: probing drivers and implications’, paper delivered to the International Sociological Association, RC43, Housing and the Built Environment Conference: Housing in an Unequal World, 15-17 September 2015, University of Illinois-Chicago, Chicago.

⁴ Tenants Union of NSW (2014) *Affordable Housing and the New South Wales Rental Market: 2014 survey report*, TUNSW, Sydney.

These data indicate the dimensions of the issue of security for private tenants: generally, private tenants are very mobile, and the large majority of moves are made for tenants' own reasons; however, a very large majority of tenants worry about their prospects *if* they had to move, a significant minority feel that they *might* have to move, and most have put up with tenancy problems for fear of adverse circumstances. This supports conceptualising 'security' in the Australian private rental sector in the way put forward by Hulse, Milligan and Easthope⁵ in their development of the concept of 'secure occupancy', which encompasses the ability of a householder to make a home of their premises. An important aspect of this sense of security is the degree of autonomy a householder enjoys in determining the conditions of their housing. In relation to rental housing, this is most obviously reflected in the degree to which a tenant feels they can remain in occupation of their premises; it is also reflected in the degree to which they feel they can ensure that the premises are maintained decently, and make their own householding decisions – such as admitting new members, decorating, or keeping pets. It is important to keep in mind this sense of autonomy in security, and not to reduce security to being fixed in occupation. Nor should mobility be confused with insecurity. A tenant who feels that unable to determine and pursue their housing interests, whether in relation to their present premises or other prospective premises – who feels stuck – is not really secure.

We can also say something about landlords. The large majority of landlords (72 per cent) own a single rental property each⁶; and most (63 per cent) declare a net rental income loss⁷ – the dominant investment strategy, therefore, is pursuit of capital gains. This strategy works best where properties can be sold not only to other landlords but also owner-occupiers, and research suggests that this is a feature of the Australian private rental sector: in a study by Yates and Wood, 40 per cent of dwellings rented privately in Sydney in 1991 had by 2001 left the rental market.⁸ Data as to how long landlords themselves stay in the market is given by Wood and Ong⁹: in a sample taken over the period 2001-06, 25 per cent of landlords exited the market within their first year; a minority (41 per cent) remained in the market continuously for five or more years.

Also, from the point of view of prospect tenant, small-holding landlords do not trade on their reputations, and neither the law nor market operates to makes them disclose much about their bona fides to prospective tenants (ie in the application process, it is always tenants, never landlords, who make applications and provide references, payslips, etc). This means for most tenants that their landlord is, at the commencement of the agreement, an unknown quantity.

These features of the sector themselves cause housing insecurity in a structural way: tenants are displaced when properties trade out of rental and into owner-occupation. Housing security could be improved structurally by addressing these features through reforms in other policy areas: for example, reforms to tax and finance settings that encourage larger-scale institutional ownership of rental properties, which may focus on steady flows of rental income rather than property dealings, have scope for managing

⁵ Hulse, K, Milligan, V and Easthope, H (2011) *Secure Occupancy in Rental Housing: conceptual foundations and comparative perspectives*, AHURI final report no 170, AHURI, Melbourne. For a brief discussion, see City Futures' previous submission: Martin, C (2016) 'Submission to the Review of the *Residential Tenancies Act 2010* (NSW)', City Futures Research Centre, UNSW, Sydney, at

https://cityfutures.be.unsw.edu.au/documents/287/RT_Act_2010_review_submission_A.pdf

⁶ ABS (2015) 'Household Income and Wealth, 2013-14', cat no 6523.0.

⁷ Australian Taxation Office (2016) 'Tax Statistics 2013-14', at <https://www.ato.gov.au/About-ATO/Research-and-statistics/In-detail/Taxation-statistics/Taxation-statistics-2013-14/?anchor=Statistics#Statistics>

⁸ Yates, J and Wood, G (2005) 'Affordable rental housing: lost, stolen and strayed', *Economic Record*, vol 81 no 255: 82-95.

⁹ Wood, G and Ong, R (2010) *Factors shaping the decision to become a landlord and retain rental investments*, AHURI final report 142, AHURI, Melbourne.

opportunities for sales and redevelopments across a portfolio, and have a reputation to protect through good service. For the purposes of the present submission, however, we leave aside the question of those structural reforms, take as given the current structure of the sector, and focus on how tenancy legal instruments and law reform can advance tenants' sense of security within the sector as structured.

Fixed terms – some basic issues and problems

In modern residential tenancies law, fixed terms are not essential: a residential tenancy agreement may, by agreement of the parties, be for a fixed term, or without a fixed term (*Residential Tenancies Act 2010* (NSW) (RTA NSW) sections 4 and 13). This differs from the historic common law requirement of leases that they be for a term of a certain duration, such that if an agreement was not for a term, it was not a lease – which led to a body of case law on what sort of term was sufficient to satisfy the requirement.¹⁰ The provision for, and use of, fixed terms under modern residential tenancies law may be seen as a hangover from the previous common law: fixed terms are unnecessary, but they are still used, but mostly for only short periods: six or 12 months.

For its duration a fixed term significantly affects rights and liabilities between the parties. For a landlord, a fixed term means that they cannot lawfully terminate the tenancy on the ground of sale (section 86) or without grounds (section 85). Because the RTA NSW does not provide specifically for termination for all the reasons landlords may have for seeking return of possession of a property – for example, where the landlord needs the property for their own housing, or the property is to be changed to a non-residential use, or where the tenancy is related to employment that has terminated – and instead leaves landlords to use without-grounds termination proceedings, a fixed term has the effect of preventing termination for all of those reasons.¹¹ A fixed term also restricts a landlord from increasing the rent: where the fixed term is for less than two years, it cannot be increased except as specifically provided for in the agreement; otherwise, where the fixed term is for two years or more, it cannot be increased more than one in 12 months (section 42).

For a tenant, a fixed term also means that they cannot lawfully terminate a tenancy – and hence their liability to pay rent to the landlord – without grounds (section 97). Because without-grounds terminations are used to cover almost all the personal reasons tenants may have for leaving a property (for example, changes in work, changes in domestic relationships, a desire for better or cheaper housing, or simply a change of scene), a fixed term has the effect of preventing lawful termination for all those reasons.¹² This also means that where a tenant terminates unlawfully, they are liable to compensate the landlord for the loss of their bargain. The amount payable depends on whether the tenancy agreement includes the optional prescribed term for a 'break fee' (section 107): if the fixed term is more than three years, the fee can be any amount as set out in the agreement; if it is three years or less, it is if it does, the fee is limited to to four or six weeks rent, depending whether the unlawful termination is effected in the first or second half

¹⁰ For example, a term 'until the end of the peanut crop' is not sufficiently certain to satisfy the requirements of a lease: *Bishop v Taylor* [1968] HCA 68.

¹¹ A very limited exception: a landlord may seek termination orders from the Tribunal where, in the 'special circumstances of the case', they would otherwise suffer 'undue hardship': section 93 RTA NSW.

¹² There are a few limited exceptions: there are specific grounds for termination where a tenant is moving into social housing or aged care (section 100(1)(a) and (b)), the landlord is selling the property (section 100(1)(c)), and in certain domestic violence situations (section 100(1)(d)), and a tenant may apply to the Tribunal for termination where, 'in the special circumstances of the case', they would otherwise suffer 'undue hardship' (section 104).

of the fixed term; and if the agreement does not contain the optional term, the liability for equivalent to rent to the end of the fixed term – subject to the landlord’s obligation to mitigate the loss (though the tenant may also be liable for losses incurred in mitigating actions, such as advertising and reletting fees).

In light of all of the above, we can characterise fixed terms as having a gross effect: they do a number of things at once, to each of the parties, and can affect the parties in a big way. In particular, they restrict landlords from a wide range of actions relating to their property ownership, and tenants from freely acting on their changing housing needs. These wide-ranging restrictions, with heavy liabilities attached, carried on for a long fixed term, makes long fixed term tenancy agreements an unwieldy instrument, both for individual landlords and tenants looking to protect their respective interests, and for policy-makers seeking to improve housing security for tenants generally.

Fixed terms and law reform – further problems

Broadly, there are two directions that law reform for long fixed terms could take. The first is that long fixed terms could be made mandatory. However, without other changes to the legal effects of fixed terms, making long fixed terms mandatory would really amount to a structural reform, effectively excluding from the sector the many landlords whose circumstances and outlook are incompatible with a long fixed term. This would be, so to speak, to take the unwieldy legal instrument and collide it head-on with the current dominant features of the sector. NSW Fair Trading is not considering taking a mandatory approach, nor does this submission support it.

The second direction is to retain the voluntary nature of fixed terms and legislatively add or subtract from their legal effects, with the intention of making them more useful. This approach has been tried before: as a result of a previous review (2005-2010) of New South Wales residential tenancies legislation, section 20 the RTA NSW gives an additional effect to a fixed term of 20 years or more: it allows contracting out of certain provisions of the Act, including the prescribed terms regarding repairs and maintenance, habitability and the landlord’s access to the premises. Section 20 does not, however, permit contracting out of the provisions of the Act regarding grounds for termination, which is where most of the restrictions of a fixed term come from. In practice, the section has not been used¹³; apparently fixed terms of 20 years, even with provision for some contracting out, remain too unwieldy.

In its report on the review of the RTA NSW, NSW Fair Trading proposes to try this approach again, by reducing the qualifying period of the fixed term to five years, and by considering whether other changes to the legal effects of a five-year fixed term should be provided for. In discussions between NSW Fair Trading and sector stakeholders, it was suggested that possible other changes might include a prescribed break fee for unlawful termination by the tenant equivalent to six weeks’ rent. We discuss each of the elements of the current proposals, and the problems we foresee, in turn.

- **The time frames.** In light of the data on the duration of landlords’ spells in the rental sector, a five-year fixed term might be a reasonable proposition for a minority – but a significant minority – of landlords. Considering the data about tenants’ mobility, and the ‘contracting-with-an-unknown-quantity’ factor, we would expect a smaller minority of tenants to be interested – except that the proposal for a prescribed break fee of six weeks’ rent very substantially and favourably limits

¹³ A ‘noteup’ search of Austlii reveals no Tribunal decisions relating to the use of section 20, and the author is not aware of any instances of its use.

tenants' liabilities relative to the fixed term. In effect, this would mean that the fixed term binds the landlord with wide-ranging restrictions for five years, but binds the tenant for only six weeks. We would expect most landlords to reject such a bargain because there is too great a risk of not actually receiving rent for the full five years; however, some might be interested in contracting on the basis of a higher rent (in effect, putting a price on the risk of early termination by the tenant). We do not think that tenants should have to pay extra for a reasonable sense of security.

- **Contracting out.** When NSW Fair Trading and the sector stakeholders discussed contracting out, they focused on the prescribed terms that obligate landlords to maintain and repair the premises – so we will focus on that too. In a way, allowing landlords to contract out of this obligation is another, less direct way of pricing a risk or cost – ie that of losing an opportunity of making money by selling or otherwise dealing with the property because of the fixed term. However, because repairs and maintenance arise at least partly from the use of premises by a tenant, we should expect market rents to be set at a level that recovers at least part of that cost from tenants. In other words, tenants effectively pay for maintenance and repairs through the rent they pay every week – even though maintenance and repairs costs are actually incurred less frequently and in varying (and sometimes large) amounts. The virtue of the current prescribed terms about maintenance and repairs is that they place the legal obligation on the party that is better placed to pay occasionally large amounts– ie the landlord, who, if the expense is large, can secure credit against their property – and thereby actually get the necessary work done, while the other party effectively pays in small amounts over time. Allowing parties to contract out of this obligation creates a new risk: not that a tenant will have to pay for maintenance and repairs (they already do, through their rent), but that they would have to pay a large amount, out of the blue, at once – and be unable to do so, so the necessary repairs and maintenance will go undone, and premises become rundown and dangerous. This is an undesirable policy outcome and inconsistent with genuine housing security.
- **Unfair contracts.** The above considerations suggest that five-year fixed term agreements with prescribed break fees and some contracting out would still not be useful for most parties; however, we are concerned that there may be instances where a tenant could be pressured by a landlord to enter into a long fixed term to the detriment of the tenant. For example, say a landlord who intends to remain in the sector knows that a current tenant wants their tenancy to continue for a long period and, because of low income or other circumstances, has few other housing options. The landlord may offer a long fixed term agreement, which contracts out of the maintenance and repairs terms and other terms to the tenant's benefit, take it or leave it (ie the tenancy is otherwise terminated). If the tenant refused to enter into the new fixed term agreement, the landlord could make good on the threat (using a without grounds termination notice), and the current provisions of the RTA NSW regarding retaliatory termination (section 115) would not protect the tenant (because the tenant has not taken or proposed to take any action – they have merely declined). This is entirely at odds with improved security.

We are of the view that provisions for long fixed term agreements, as proposed, would in most cases not be useful, and where they are used may be used unfairly to the detriment of vulnerable tenants.

Fixed terms should be regarded as a hangover of the common law of leases, and not as an essential – or even very useful – part of a modern legislative scheme for residential tenancies. Law reforms regarding grounds and notice periods for terminations, and regarding rent increases, represent the better way forward: this avoids the problems of the unwieldiness and grossness of effect of fixed terms, works within

the current structures of the sector, and more precisely and effectively gets at improving housing security for tenants.

A better way – law reform regarding termination grounds and notice periods, and rent increases

In our previous submission we recommended law reform for the removal of without grounds terminations by landlords (including at the end of a fixed term without), and for the creation of additional specific grounds for termination by landlords. These grounds would be:

- that the landlord or a family member needs the premises for their own housing;
- that the tenancy is directly related to the tenant's employment by the landlord or associated entity, and the employment is terminated; and
- that the premises are to be renovated, demolished or changed to a non-residential use;

These new grounds would sit alongside the specific grounds already available to landlord – sale (section 86) and breach (section 87 and 88) – and the provisions for termination by the Tribunal (sections 90-93). We also recommended that in all termination proceedings by landlords the Tribunal should have discretion as to whether to order termination, considering the circumstances of the case. As we said in that submission, these reforms would improve security for tenants – including in the assertion of their rights – without restricting their mobility, and would accommodate the reasonable interests of landlords currently operating in the sector. We remain of the view that this is the better way to improve tenants' security.

In contrast to long fixed terms, this approach is more nuanced, with the different degrees of urgency in landlords' reasons for seeking termination reflected in the different periods of notice for termination, and in the exclusion of some grounds during a fixed term (as the sale ground is currently excluded, so would the 'landlords' own housing' and 'change of use' grounds be excluded during a fixed term). The principle of this nuanced approach could be taken further, by providing for prescribed exclusion periods of different lengths, reflecting differences in the grounds. For example, the 'landlords' own housing' ground could be excluded for the first six months of a tenancy (or the length of the fixed term, whichever is the longer), while the 'sale' ground could be excluded for the first 12 months (or length of fixed term, whichever is longer) and the 'change of use' grounds could be excluded for the first 18 months (or length of fixed term, which is longer), to reflect a policy priority for housing persons over the pursuit of development opportunities.

A further variation on this scheme could be considered, to provide for some flexibility in particular cases. Provision could be made for a shorter exclusion period to apply if, before the agreement is made, the landlord discloses to the prospective tenant that the landlord genuinely and presently has the intention to use that ground to terminate the tenancy. So, for example, a landlord who lets their own home while holidaying for three months could disclose their intention to move back in and reduce the exclusion period from six months (as suggested above). We note that it would not be possible for landlords to use such a provision to reduce or avoid all the exclusion periods, because a disclosure that they intend to use the premises as their home, and sell the premises and change their use is contradictory on its face and does not disclose a genuine present intention.

Finally, applying exclusion periods to rent increases would also improve security. We recommend that rent increases should be excluded in the first 12 months of a tenancy, and for a 12-month period following a rent increase.