Client Newsletter

No. 1, 2005

In touch with the law

The law is constantly changing and this newsletter describes developments which may be relevant to you. If you are in any doubt about these or any other aspects of the law, please make an appointment to see your solicitor.

DEPRECIATING ASSETS
What can be claimed for rental property?

This is an issue close to the hearts – or at least the pockets – of many taxpayers, particularly given the large number of investors who own rental properties which are negatively geared.

The Tax Office has issued a new ruling on what constitutes 'depreciable plant' in residential rental property. It is doing this to delineate what is not plant, as it seeks to reduce the amount of deductions claimed by property investors.

The best result for the investor is that any property acquired – such as alterations or improvements – qualify for the more favourable depreciation rate attracted by plant.

As a guide, there is a presumption that the premises and any associated fixtures and fittings are not plant – for instance, kitchen cupboards, insulation batts and built-in wardrobes are not plant, and therefore not depreciable.

The Tax Office carries out a number of tests: the setting, function, and completeness tests. Something which is merely the setting in which the taxpayer's income-producing activities are carried on is not plant.

Where an item is more than mere setting, it must satisfy the function test to qualify as plant. The function performed by the item must be so closely related to the taxpayer's income-earning activities, or so special, that it warrants being regarded as plant.

Also, whether a building would be complete without a particular item aids in the determination of whether an item is plant, but this is not a conclusive test.

Machinery is plant, even if it forms part of the setting – for example, air-conditioning equipment, dishwashers, stoves, range hoods and burglar alarms. Ducting and piping do not qualify, unless they are truly part of a machine, and not merely joined to it. Consult your solicitor if you would like further information. ❑

UNCONSCIONABLE CONDUCT
Mall management in leasing dispute

A simple 'stuff-up' over the permitted-use provisions and exclusivity rights of two Bangladeshi traders in the Minto Mall could have been sorted by normal commercial negotiation, according to a recent decision by the Administrative Decisions Tribunal.

The mall landlord had leased one shop to sell "Indian groceries" and the other to be conducted as "an Asian grocery shop".

When a dispute arose over exclusivity, the landlord tried to argue that India was not in Asia. Then it sought to remove one of the traders by embarking on a course of what the ADT termed "unconscionable" conduct.

This included exerting undue pressure or influence on the tenant, requiring the tenant to comply with conditions not reasonably necessary to protect the landlord's interests, unreasonably failing to let the tenant know the risks associated with intended conduct by the landlord and not acting in good faith.

The ADT said, "We consider the (landlord's) conduct to be quite unacceptable in the ordinary management of a retail shopping centre having regard to usual industry standards and practices". ❑

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FINE PRINT

Contractor bound by unread terms in contract

The recent case of a pharmaceutical supplier bound by the courts to the terms of a contract it had neglected to read is a salutary reminder of the need to always read the fine print and never sign a contract till you have had proper legal advice.

In this case, company A was a supplier of flu vaccine to customers across Australia through a sub-distribution arrangement with the drug's South Pacific distributor. The distributor's Australian subsidiary, company B, looked after the collection, storage and regulatory approval for the vaccine.

Company B had arranged for the vaccine to be stored at transport company C's warehouse in Sydney, then delivered across Australia. However, the operations manager of company B had failed to read the conditions of contract on the back of the transport company's credit form.

The conditions included that customers and their associates, not the transport company, were responsible for any loss or damage and for taking out insurance.

After the transport company collected over 70,000 doses of vaccine from the airport, company A inspected the goods at the warehouse. When temperature monitors were inserted, most of the drugs had to be rejected because they had become too cold and could not be used.

Company A took the position that conditions on the credit application form were not part of the contract, but the High Court decided they were, and that company B was acting as company A's agent in contracting for the services of the transport company.

The Court reaffirmed that a party which has signed a written contract is bound by its terms, whether it has made itself aware of them or not.

The court explained that the rights and liabilities of parties to a contract are determined by what a reasonable person would understand them to mean, not by the understanding of the parties themselves. ❑

PAPER TRAIL

What documents should a business keep?

In a well-publicised court case, a tobacco company was told by the judge that its destruction of documents had made a fair trial impossible. The judge's decision against the company was overturned on appeal, but it alerted the business world to be very careful about its obligations for document retention.

All businesses are governed by strict rules for retention of financial records for taxation purposes, and some have particular legal requirements or codes of conduct that determine how long they have to keep other documents. Beyond this, before destroying any document a business should assess whether it could be required for any possible future litigation and whether its destruction could lead a court to draw an adverse inference.

Some businesses are more liable to face litigation than others. A business should consider the relevant statutory limitation period. If you are a manufacturer, establish the life expectancy of a product, determining how late a personal injury could occur, then add the appropriate limitation period, with a couple of additional years for unforeseeable events. Keep documents for that length of time.

Statutory limitation periods are only a guide. Some documents should be held longer. For instance, the Australian Standard on document retention recommends that documents of simple contracts should be kept for at least seven years from the date the contract terminates. Only if no notice for breach of contract is served within the seven years should records be destroyed. If there is a dispute, records should be retained for a further seven years beyond settlement, or longer if a judgment is necessary to settle the dispute. Similarly, documents about the design, development, or materials in goods manufactured for sale, should be retained.

Any destruction of records will 'look better' should a business become involved in litigation, if it results from a consistent policy rather than ad hoc decisions.

Speak to your solicitor if you would like further details of your obligations or help in developing a document retention policy. ❑

VENDOR DUTY

New charge on land-rich entities

A new vendor duty on sales of an interest in a 'land-rich landholder' has been imposed retrospectively from 10 November 2004.

The new charge follows the introduction of vendor duty on the sale of some classes of property in NSW on 1 June last year, and is in addition to land-rich duty already payable at rates of up to 5.5 per cent by a purchaser who makes a relevant acquisition in a land-rich landholder.

Vendors disposing of an interest in a land-rich landholder are now liable to an additional duty at 2.25 per cent.

A vendor will be caught by the new duty if they have a significant interest in the landholder, or had such an interest anytime within the three years preceding the sale.

The duty doesn't apply if the disposal follows an agreement entered into before the date of the budget announcement last May.

A landholder is land-rich if they have land holdings in NSW with an overall value of $2 million or more, and their land holdings everywhere, whether inside or outside Australia, total at least 60 per cent of the unencumbered value of all their property.

A landholder can be a private company, a private unit trust scheme or a wholesale unit trust scheme.

The relevant criterion for the imposition of duty is the size of the interest held by the vendor, rather than the size of the interest disposed of.

Some transactions will now be subject to land-rich duty which were not previously.

There are exemptions; for example where the transfer of land would have been exempt from vendor duty by virtue of an exemption for farms, improved vacant land, and new or substantially new buildings. There are also exemptions which correspond to those currently available for land-rich purchaser duty.

Significantly for the property industry, there is a lack of exemptions for the syndication of interests in a unit trust scheme. ❑

STAFF SURVEILLANCE

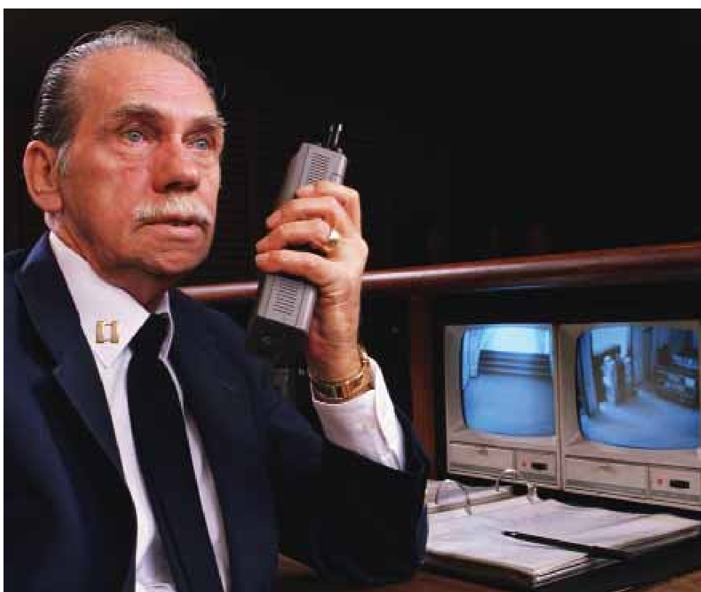
Legal requirements must be followed

Nine security officers have been reinstated with back pay after an unfair dismissal case rejected the employer's claim that they had engaged in serious misconduct. The employer of the nine had relied on covert video surveillance of the officers by outside agents.

Employers are required to obtain authority from a magistrate for such surveillance. In this case the employer had breached the Workplace Video Surveillance Act by carrying out much of the surveillance before obtaining an authority, and then by conducting the surveillance outside its specifications.

The Industrial Relations Commission, which found the nine had been unfairly dismissed, described the surveillance as having the hallmarks of "a Keystone Cops episode".

In carrying out surveillance, an employer must conform with the requirements of the Surveillance Act, gaining permission from a magistrate beforehand and providing reports as required. It is also necessary to carefully re-examine the surveillance report and conduct further investigations to confirm its findings before acting on them, particularly where they are being used to justify dismissal. ❑



DIRECTORS

If you act for a company, you can be liable too

An individual director acting in trade or commerce on behalf of a company also acts for himself or herself. If the company is liable, the director is equally liable.

This Federal Court ruling follows on a case where the director of a company that was selling a bakery made misleading statements about the profitability and value of the business.

The purchaser was told the net profit for the business was $169,716 on "actual figures", whereas only $56,693 was recorded on accounts that finally came to light in court.

After the sale, the bakery failed to trade profitably and was closed. The former owners put this down to the new owner's lack of management skills. But when the purchaser found that a director of the company selling the business had misrepresented reality, she sued the company and its directors for damages.

One director admitted that all the conduct attributed to the company was his, and the judge awarded damages to the purchaser. The judge said the purchaser had relied on the misleading information to buy the business.

The director had engaged in misleading conduct in trade or commerce under the Trade Practices Act and under the Fair Trading Act.

Under the Trade Practices Act, the director of a company has liability as an accessory if they knew what was going on. Under the Fair Trading Act, if they act for a company they act for themselves and have primary liability. ❑

RETAIL TENANTS

Lease costs shift to landlords

Recent changes to the law make it an offence for landlords to recover lease preparation expenses to which they are not entitled.

If a landlord contravenes the relevant parts of the Retail Leases Amendment Act 2004, they will be guilty of an offence and liable to a penalty of up to $11,000.

The tenant will also be able to recover, as a debt from the landlord, any payment accepted by the landlord in contravention of the law.

Prior to the new law, it was an offence for a landlord to accept 'key money' for granting renewal or extension of a retail shop lease, but they could require the tenant to pay a reasonable amount for legal or other expenses associated with preparing entry into, renewing or extending a retail shop lease.

Accepting key money is still an offence. Now, however, the landlord must pay for lease preparation expenses.

A lease will be voided to the extent that the tenant has had to pay key money or preparation expenses connected with granting, renewing or extending the lease.

Preparation expenses include legal costs and associated disbursements like company search fees and photocopying fees; fees for preparing survey plans and mortgage consent fees.

A small concession

The landlord may recover lease preparation costs if the tenant asks for amendments to the lease – but not when the amendments are:

❑ to insert or vary the tenant's particulars, the rent or the term;
❑ to remedy the landlord's failure to include or omit a term that both parties had agreed on;
❑ or the amendments are requested before the tenant has given the landlord a disclosure statement or a tenant disclosure update.

Where the tenant is liable to pay for amendments to the lease, the landlord must give them a copy of any accounts received for expenses arising from the amendments.

To minimise exposure to additional lease costs arising out of a tenant's requests for amendments to the lease, landlords should require that the tenant provide their disclosure statement prior to the submission of lease costs.

No more six-monthly statements

A second important change removes the requirement that the landlord should make available to a tenant every six months a document detailing all landlord expenditure on outgoings to which the tenant contributes.

The statement will still have to be given before a lease is entered into, but thereafter only once a year. ❑

REAL ESTATE COMMISSIONS

Agents' retainers must be in writing

Despite criticism from judges that the law can be harsh and unfair in the way it operates against 'reasonable' agents who fail to have a written agreement with clients, there's no relenting: real estate agents must put their retainers in writing.

A recent change has introduced some flexibility, though not a great deal. As the law currently stands, where a copy of an agreement is not served within the required time, a commission or expense may be claimed only if a judge is satisfied that:

❑ the delay was inadvertent;
❑ the commission or expense is fair and reasonable; and
❑ disallowing the claim would be unjust.

But agents will still be unable to recover or retain a commission unless:

❑ an agreement has been made in writing;
❑ the agreement complies with Regulations; and
❑ the agreement is concluded before services are rendered.

In a case last year, an agency which merged its operations with another and failed to sign a new agreement with a client was ordered by a Tribunal to repay the commissions it had retained and, moreover, pay damages for breaching the very same management agreement the Tribunal said it had failed to sign with the client. ❑

This newsletter is for the benefit of our clients. It is not intended to be a definitive analysis of legislative or other changes and professional advice should be taken before any course of action is pursued