

Key-Money

What is Key-Money?

'Key-money' is defined in section 3 of the *Retail Leases Act 2003* (the '**Act**') as follows:

key-money means money that a tenant is to pay, or a benefit that a tenant is to give, that is—

- (a) by way of a premium, or something similar in nature to a premium, in that there is no real consideration or no true consideration given for the payment or benefit (for example, it is so disproportionate to the benefit that it cannot be true consideration); and
- (b) in consideration of—
 - (i) a lease being granted or an agreement being made to grant a lease; or
 - (ii) the variation of a lease; or
 - (iii) the renewal of a lease or the granting of an option for the renewal of a lease; or
 - (iv) consent being given to the assignment of a lease or to the sub-letting of the premises to which a lease relates

Key-Money is prohibited

Section 23(1) of the Act prohibits seeking or accepting the payment of key-money or any consideration for the goodwill of any business carried on at the retail premises.

This prohibition applies to landlords, prospective landlords and anyone acting on their behalf (section 23(5) of the Act).

Contraventions of the prohibition are punishable by a fine of 50 penalty units (section 23(1) of the Act).

A provision in a retail premises lease is void to the extent that it requires the payment of key-money or consideration for goodwill, or has that effect (section 23(2) of the Act).

This means that if a provision in a retail premises lease or other agreement requires payment of key money either:

- it is unenforceable; or
- if key money has been found to have been paid, the tenant can recover the payment and the landlord is liable for a fine.

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Examples of potential key money issues include:

Example 1

A landlord is seeking the payment of \$10,000 from the tenant before the landlord will provide access to the tenant at lease commencement. The payment is likely to constitute key money and be prohibited by the Act.

Example 2

A landlord agrees to consent to the assignment (i.e. transfer) of a lease to a new tenant provided that the existing tenant first pays \$20,000 to the landlord. If the existing tenant receives nothing in return for the payment other than the landlord's consent to the assignment, the payment is likely to constitute key money.

Example 3

A tenant who is in arrears requests an assignment to a new tenant. The landlord agrees to the assignment if the new tenant pays the arrears owed by the tenant requesting the assignment. Such a payment is almost certainly key money. However, it would not constitute key money if the payment was required from the existing tenant.

Recovery of key-money

Section 23(4) of the Act provides that any payment made, or the value of any benefit conferred, by the tenant and received by the landlord in contravention of the prohibition of key-money or consideration for goodwill may be:

- (a) recovered by the tenant from the landlord in a court of competent jurisdiction as a debt due; or
- (b) otherwise recovered by the tenant from the landlord as determined under Part 10 of the Act (Dispute Resolution).

What is not key-money?

The Act recognises a need to balance:

- (a) the protection of tenants from being coerced by landlords or their associates to make key-money payments; and
- (b) the commercial reality that in the course of business relations between a landlord and tenant, some payments may be required.

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A number of exceptions from the prohibitions on key-money payments are contained within section 23(3) of the Act. Specifically, under section 23(3) of the Act, a landlord is not prevented from:

- (a) recovering from the tenant costs which the landlord reasonably incurred in investigating a proposed assignee of the lease or sub-tenant of the premises;
- (b) recovering from the tenant costs which the landlord reasonably incurred in connection with:
 - (i) an assignment of the lease or a sub-lease; and
 - (ii) obtaining any necessary consents to the assignment or sub-lease;
- (c) claiming goodwill from the tenant in relation to the sale of a business that the landlord operated from the retail premises immediately before its sale, if the lease was granted to the tenant in the course of the sale of the business;
- (d) receiving payment of rent in advance;
- (e) securing the performance of the tenant's obligations under the lease by requiring a bond, security deposit or guarantee to be provided from the tenant or any other person (such as a requirement that the directors of a corporation guarantee performance of the corporation's lease obligations);
- (f) seeking and accepting payment for plant, equipment, fixtures or fittings that are sold by the landlord to the tenant in connection with the lease being granted; or
- (g) seeking and accepting payment for the grant of a franchise in connection with the lease being granted.

Legal or other expenses

Section 51(1) of the Act provides that a landlord cannot claim from any person (including the tenant) the landlord's legal or other expenses relating to:

- (a) the negotiation, preparation or execution of the lease;
- (b) obtaining the consent of a mortgagee to the lease; or
- (c) the landlord's compliance with the Act.

Section 51(2) of the Act provides that sub-section (1) does not prevent a landlord from claiming the reasonable legal or other expenses incurred by the landlord in connection with an assignment of the lease or a sub-lease, including investigating a proposed assignee or sub-tenant and obtaining any necessary consents to the assignment or sub-lease.

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Therefore, on an assignment or sublease the landlord can claim these expenses from the tenant to the extent that they are reasonable and provided that the landlord and tenant have agreed that the landlord's expenses will be payable by the tenant.

Example 1

A landlord engages an agent and a lawyer to undertake the work necessary to enable the tenant's assignment of lease to proceed. The landlord and tenant have agreed in the lease that the tenant must reimburse the landlord for the landlord's reasonable costs upon an assignment of lease. The landlord seeks to pass on to the tenant the fees, calculated on an hourly rate basis for the work done, charged by the estate agent and the lawyer.

Provided that the fees charged are reasonable, these charges are unlikely to be contrary to the prohibition on key-money and consideration for goodwill. By contrast, a fee calculated on the basis of a fixed percentage of the rent is very likely to constitute key money.

Example 2

A lease requires the tenant to pay \$10,000 on lease commencement. At that time the landlord transfers to the tenant ownership of plant, equipment, fixtures and fittings located in the premises. The Act allows a landlord to accept payment for plant, equipment, fixtures or fittings that are sold by the landlord to the tenant in connection with the lease being granted. A sale of this sort should be recorded in the lease.

Example 3

A landlord requires a tenant to pay \$90,000 for the 'locational goodwill' associated with a premises. This is on the basis that the premises are a 'landmark hotel' and so attract 'locational goodwill' in the sense that because it is well known it attracts a high number of patrons and the tenant should be required to pay for this. The payment is likely to contravene the prohibition upon requiring payments for goodwill and therefore amount to key-money. The Act allows a landlord to require a tenant to pay goodwill only in relation to the sale of a business that the landlord operates from the premises immediately before its sale in circumstances where a lease is granted to a tenant in the course of the sale of the business.

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Resolving disputes concerning key-money and consideration for goodwill

The Office of the Victorian Small Business Commissioner (**VSBC**) offers a dispute resolution service to assist parties to resolve business disputes. A dispute can be referred to the VSBC by submitting an application which summarises the issues and specifies the parties involved. Application forms can be found at: <http://www.vsbv.vic.gov.au/homepage/notify-a-dispute-or-apply-for-mediation>

The Small Business Commissioner (**Commissioner**) appoints an officer to consider the application, contact the parties and, through providing preliminary assistance, seeks to resolve the dispute. There is no cost to the parties for this service. If the dispute cannot be resolved at this stage, the parties are invited to attend mediation.

Mediation involves a meeting between the parties in dispute and an independent mediator who will attempt to assist the parties to reach an agreement about the dispute. When all parties agree to mediation, the Commissioner appoints a mediator and the VSBC arranges the date, time and venue. The mediation can be in regional Victoria if it is more convenient for the parties. Mediation costs only \$195 per party per session and usually takes 3-4 hours.

The mediation is confidential. However, any settlement agreement may be taken to the Victorian Civil and Administrative Tribunal (**VCAT**) or an appropriate Court for enforcement, if necessary.

Each party pays their own costs at VCAT. However, where a party refuses to take part in mediation under the Act, VCAT has the power to order that party to pay the costs of the other party.

Further information, including the cost of mediation can be found on the VSBC's website at www.vsbv.vic.gov.au

Further Information

Contact the Office of the Victorian Small Business Commissioner

Call **13 VSBC (13 8722)**

TTY **(03) 9651 7596**

Or visit: www.vsbv.vic.gov.au

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