

ISSUES PAPER:

DEVELOPMENT OF A CENTRAL BOND HOLDING SCHEME IN THE NORTHERN TERRITORY

UNDER THE

RESIDENTIAL TENANCIES ACT

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1 Introduction

All other Australian jurisdictions have mandatory rental deposit systems, except for the Northern Territory. Whilst this topic has been the subject of ongoing discussion for more than a decade in the Territory, the status quo has been maintained in spite of impetus from a number of sources to move to establish a scheme.

The purpose of this paper is to seek comment from the public on a proposal to establish a rental deposit authority in the Northern Territory. This has arisen following an identified need to promote fair and equitable dealing between property owners and tenants in the disbursement of the rental deposit.

This paper addresses the likely impact that the proposal will have on the residential tenancy market.

Given that there is no single Territory-wide tenancy advisory service or a tenants or landlords association, it is difficult to obtain general views and comments as to whether a centralised bond holding scheme is required from the major stakeholders which are landlords and tenants.

This paper attempts to solicit such views.

The paper provides industry, members of the public, the regulatory authorities and the government with an overview of:

- the current legislation and its background;
- regulatory developments that have occurred elsewhere in Australia; and
- options for change and reform.

This overview should provide enough background information to support submissions as to what should be the policy outcomes concerning the issues raised in this Issues Paper.

2 Consultation

You are invited to provide comments on this issues paper to the Department of the Attorney-General and Justice. Comments can be as short or informal as an email or letter, or it can be a more substantial document. Comments do not have to address all aspects of this Issues Paper. Electronic copies should be sent whenever possible.

Comments should be sent to:

Director, Legal Policy
Department of the Attorney-General and Justice
GPO Box 1722,
DARWIN NT 0801

Or by email to Policy.AGD@nt.gov.au

The closing date for comments on this Issues Paper is 30 April 2015.

Any feedback or comment received by the Department of the Attorney-General and Justice will be treated as a public document unless clearly marked as 'confidential'. In the absence of such clear indication, the Department of the Attorney-General and Justice will treat the feedback or comment as non-confidential.

Non-confidential feedback or comments will be made publicly available and published on the Department of the Attorney-General and Justice website. The Department of the Attorney-General and Justice may draw upon the contents of such and quote from them or refer to them in reports, which may be made publicly available.

Any requests made to the Department of the Attorney-General and Justice for access to a confidential submission, feedback or comment will be determined in accordance with the *Information Act* (NT).

Note: Although every care has been taken in the preparation of the Issues Paper to ensure accuracy, it has been produced for the general guidance only of persons wishing to provide comments on the issues. The contents of the paper do not constitute legal advice or legal information and they do not constitute Government policy documents.

3 Current Position

3.1 Background

The *Residential Tenancies Act* was enacted in 1999, following a long period of extensive community consultation.

The Act aims to provide a framework which enables parties to residential tenancy agreements to interact with clear and consistent guidelines. The Act aims to present, in a logical structure, a set of rules governing residential tenancies so as to reduce disputes between the parties. In the event of a dispute, the Act establishes a streamlined and easily accessible dispute resolution process.

The Act sets out the minimum terms of residential tenancy agreements, and sets out the procedures relating to security deposits, condition reports and payment of rent. It clarifies the respective rights and responsibilities of tenants and landlords in respect to repairs and maintenance of the premises, and sets out the rules for the termination of a tenancy by a tenant or landlord.

The Act is administered by the Commissioner of Tenancies¹, who is provided with wide ranging powers in respect of conciliation and inquiry, and the making of enforceable orders. The Commissioner is also responsible for the enforcement of the Act, which includes the power to issue infringement notices for certain breaches of the Act.

The jurisdiction of the Commissioner is similar to that of the Small Claims Court, with more significant or complex issues being matters for the Court (usually the Local Court) to determine.²

Within this framework, the objectives of the Act (which are set out in section 3) are:

- to fairly balance the rights and duties of tenants and landlords;
- to improve the understanding of landlords, tenants and agents of their rights and obligations in relation to residential tenancies;
- to ensure that landlords and tenants are provided with suitable mechanisms for enforcing their rights under tenancy agreements and the Act;
- to ensure that tenants are provided with safe and habitable premises under tenancy agreements and enjoy appropriate security of tenure; and
- to facilitate landlords receiving a fair rent in return for providing safe and habitable accommodation to tenants.

The Act has been amended a number of times since 1999, addressing mostly technical issues surrounding the handling of security deposits, termination and notices of unpaid rent, and condition reports.

¹ Who, by virtue of section 13, is the Commissioner of Consumer Affairs.

² The Commissioner has jurisdiction to hear monetary claims up to \$10,000.

A significant change to the Act occurred in 2006, with the introduction of Acceptable Behaviour Agreements for public housing tenants, and provision for third parties to apply to the court for termination of a tenancy for unacceptable behaviour.³

Under these amendments, the Department of Housing is able to compel a tenant to enter into an Acceptable Behaviour Agreement (where the tenant agrees not to engage in antisocial behaviour at the premises).

If the tenant fails to sign an agreement, or breaches the agreement, the Department of Housing may seek an order from the court terminating the tenancy.

3.2 Central Bond Holding Schemes - Australian jurisdictions

Queensland, New South Wales, South Australia, Victoria, Western Australia, Tasmania and the Australian Capital Territory have each established a Bond Board or Authority to hold security bonds on behalf of tenants.

Each board/authority has functions that are much broader than collecting and disbursing bond money. The various Residential Tenancies Acts provide for the investment of bond money and permits the board/authority to apply the interest generated through that investment to meet the cost of administering the bond scheme, including dispute resolution services and the provision of educational material and sessions. Some schemes also extend to providing funding for accommodation and public housing needs.

In addition to managing bond monies, the various boards/authorities provide conciliation/dispute resolution services, conduct public awareness campaigns and produce educational material on tenancy matters. The boards/authorities also provide advice to the government/minister on matters relating to the residential tenancy market.

3.3 The Situation in the Northern Territory

The Northern Territory remains the last jurisdiction in Australia to legislate the establishment of central bond holding scheme.

Tenants' bond monies within the Northern Territory are currently held by landlords, or their agents, with the interest income generally retained by either the landlord or agent.

Should there be a dispute over the bond, the tenant must lodge an application with the Commissioner of Tenancies to seek return of their bond monies⁴. While it is anticipated that the newly constituted Northern Territory Civil and Administrative Tribunal will take over hearing responsibilities from the Commissioner in early 2015, that transfer will not influence current practices and issues relating to the management and retention of bond monies.

³ *Antisocial Behaviour (Miscellaneous Amendments) Act 2006*

⁴ Section 113 *Residential Tenancies Act*

3.4 The role of security deposits (i.e. bonds) in the rental property market

Most property owners in the residential tenancy market require security deposits from tenants⁵. The purpose of such deposits is to reduce the risk of loss to the owner arising from a default by the tenant. Such defaults include the non-payment of rent and physical damage to property. Loss may include loss of rent and other costs arising from a tenant's departure prior to the expiry of a fixed term agreement.

3.5 Other countries

Security deposits are a common feature of contemporary rental markets in the United States, Great Britain, New Zealand and Canada. New Zealand and Great Britain have some restriction on the amount of security deposits and other up-front charges. In New Zealand, bonds must be lodged with the Ministry of Business, Innovation and Employment. Various jurisdictional tenancy deposit schemes operate in Great Britain. The New Zealand and British schemes incorporate dispute resolution systems.

In the United States, 27 of the 51 States have some form of restriction on the value of a security deposit, with disputes arbitrated in tenancy tribunals or mediation boards. In Canada, most Provinces have some restriction on the amount of security deposit, however security deposits are prohibited in Quebec and in Ontario, landlords are limited to seeking the last month's rent up front. There are no bond repositories in Canada however the Provinces have publicly funded dispute resolution systems.

3.6 The Northern Territory Residential Rental Market

Housing is a basic human necessity and affects everyone in our community. The Northern Territory has some unique aspects and challenges facing its housing market, and its rental housing market is no exception. According to the 2011 Census, the Northern Territory has the highest rental housing rate in the country per capita with 49.1% of all occupied dwellings being rented (amounting to 29,903 dwellings) with over half located in the Darwin region (16,239 dwellings). By comparison, the Australian average rental rate is only 29.6%⁶.

Of those rented dwellings in the Territory, 29.1% were rented through a real estate agent, 25% were rented from the Territory Government and 45.9% were rented from other landlord types (namely, private landlords). Again, this contrasts with the rest of Australia where 54.3% were rented through a real estate agent, 13.7% from a state or territory housing authority and 32%⁷ from other landlords.

In addition to the high proportion of rental housing amongst occupied dwellings, the Territory's rental affordability index is the highest in the nation at 35.8% of income in comparison to the Australian average of 25.6% and the next highest ratio of 28.3% in

⁵ Security deposits are not mandatory under the *Residential Tenancies Act*, however if a tenancy agreement contains a bond provision, Parts 5 and 12 of the Act will apply to the security deposit.

⁶ ABS Community Profiles

⁷ ABS Community Profiles

Sydney⁸, despite the Territory's average weekly earnings being above the national average⁹.

Against a setting of high income, the Territory's rental affordability index is driven by high rental costs, with for example the mean house rental price of \$663 in Darwin set against the next highest rate of \$510 in Sydney for the September quarter 2014 (\$505 in Alice Springs and \$485 in Katherine)¹⁰.

It is this particular aspect of the statistics that influences the discussion over the establishment of a central bond holding scheme. With residential tenancy bonds legislated at a maximum of 4 weeks rent, the average size of a bond is \$2,652; over double the average weekly wage.

In December 2011, the National Housing Supply Council released its 'State of Supply Report' which found that, relative to the size of its market, the greatest shortfall of housing in Australia is in the Territory, where the Council estimates the shortfall to exceed 10% of total underlying demand. While recent housing developments have added to housing stock overall, vacancy rates remain at low levels: ranging from 0.3% in Katherine to 6.7% in Darwin for houses; and averaging just over 3% for units in Darwin and Palmerston¹¹.

With a historical tendency for high turnover of the population¹² and a growing population base, a shortage of housing stock and constant demand for rental properties can place upward pressure on rental prices and reduce the comparative bargaining power of tenants, as more tenants compete for rental properties. High rental prices, and thus bonds, will continue to place considerable housing stress on low income earners in our community.

3.7 The current regulatory system

Residential tenancies are regulated under the *Residential Tenancies Act*.

Under the *Residential Tenancies Act*¹³, a 'bond' is defined as:

"a provision of a tenancy agreement or an agreement collateral to a tenancy agreement under which a tenant is required to give a security deposit for the performance of obligations under the tenancy agreement."

The term 'security deposit' is defined as:

"an amount of money a tenant has paid, or is required to pay under a bond."

⁸ Economics Brief – Home Loan and Rental Affordability – September 2013; Northern Territory Department of Treasury and Finance

⁹ ABS Time Series Catalogue 6302 (Australia : \$1 123; Northern Territory \$1 198)

¹⁰ Territory Economic Review – November 2014 – Department of Treasury and Finance

¹¹ Territory Economic Review – November 2014 – Department of Treasury and Finance

¹² ABS: Regional Statistics, Northern Territory, March 2011 (cat. no. 1362.7)

¹³ *Residential Tenancies Act* (NT) s.4

3.7.1 Part 5, Division 2 of the *Residential Tenancies Act*: Bonds and security deposits

Part 5, Division 2 of the *Residential Tenancies Act* sets out a number of rules to be followed by landlords and tenants with respect to the payment and management of bond moneys.

In summary these include:

- a landlord cannot require payment of a bond that is greater than 4 weeks of rent¹⁴;
- bond money paid to a landlord is held by the landlord in trust for the tenant¹⁵;
- the landlord must pay the bond money into a real estate agent's trust account or the account of the landlord with a bank, building society etc¹⁶;
- if the landlord is holding the bond money and intends to leave the Territory for a period greater than 14 days, the landlord must pay the bond money to a real estate agent or to a person approved in writing by the Commissioner of Tenancies and notify the tenant of the name of who is holding the moneys¹⁷;
- a landlord must provide a receipt to the tenant immediately after the bond money has been paid¹⁸;
- a landlord must on the written request of a tenant give the tenant a statement in relation to the bond money which sets out amongst other things the account in which the bond money has been deposited, the amount of the bond money being held in the account, and the date the money was paid into the account¹⁹.

3.7.2 Part 12, Division 2: Return of security deposit and interest

Part 12, Division 2 of the *Residential Tenancies Act* sets out a range of rules in relation to the return of bond moneys at the end of a tenancy.

In summary these include:

- a tenant is entitled to have his/her bond money reimbursed to him/her no later than 7 days after the end of the tenancy²⁰;
- at the end of the tenancy, a landlord is entitled to retain some of the bond money in order to make good damage caused to the premises, replace property lost or destroyed by the tenant, clean the premises if left unreasonably dirty by

¹⁴ *Residential Tenancies Act* (NT) s.29(1)(a)

¹⁵ *Residential Tenancies Act* (NT) s.29(3)

¹⁶ *Residential Tenancies Act* (NT) s.29(4)

¹⁷ *Residential Tenancies Act* (NT) s.29(5)

¹⁸ *Residential Tenancies Act* (NT) s.31

¹⁹ *Residential Tenancies Act* (NT) s.32

²⁰ *Residential Tenancies Act* (NT) s.112(1)

the tenant, pay for unpaid rent or for other prescribed reasons²¹. Before a landlord can retain bond moneys, a tenant must accept a condition report relating to the premises;

- the landlord cannot retain moneys to make good damage caused to the property and the like unless the landlord serves a notice with the prescribed information (i.e. a notice of intention to retain bond moneys that is supported by a statutory declaration attesting to the reasons and evidence supporting the intended retention) on the tenant²²;
- a tenant may apply to the Commissioner of Tenancies for the return of some or all of the bond money and interest²³;
- interest on bond moneys (other than bond moneys held in real estate agents accounts which are retained by the agent²⁴) are paid to the person specified in the tenancy agreement (ie. the landlord or the tenant) or if not specified, then to the party who is entitled to the greater portion of the bond money²⁵;
- the Commissioner of Tenancies deals with disputes relating to bond moneys.

3.7.3 Agents Licensing Act

Section 50 of the *Agents Licensing Act* sets out requirements for agents when opening trust accounts.

This section provides that the arrangements that normally apply to agents, where interest earned on moneys in the trust account are paid into the Agents Licensing Fidelity Guarantee Fund, do not necessarily apply with respect to interest earned on trust moneys that are bond moneys.

This interest is retained by the agent in the absence of an application under the *Residential Tenancies Act*.

3.7.4 Codes of Practice

Part 13 of the *Consumer Affairs and Fair Trading Act* (CAFTA) permits the making, as Regulations, of Codes of Practices. Such Codes are developed by the Commissioner of Consumer Affairs in consultation with the relevant industry and the public.

There have been no codes of practice established under Part 13 of CAFTA regarding landlords and tenants.

²¹ *Residential Tenancies Act* (NT) s.112(4)

²² *Residential Tenancies Act* (NT) s.112(5)

²³ *Residential Tenancies Act* (NT) s.113

²⁴ *Agents Licensing Act* (NT) s.50

²⁵ *Residential Tenancies Act* (NT) s.114

3.7.5 Who is affected by the legislation?

Every person involved in a residential tenancy transaction in the Northern Territory is affected by the legislation.

It should however be noted that there are some limited exemptions set out in section 6 of the *Residential Tenancies Act*, including mobile homes and caravans situated in caravan parks.

4 Historical overview of Northern Territory legislation relating to Residential Tenancy Bonds

4.1 Legislative development

Prior to the commencement of the *Residential Tenancies Act* on 1 March 2000, residential tenancies were regulated under the *Tenancy Act 1979*.

Whilst that Act dealt in part with the issue of residential tenancy bonds, protection mechanisms for tenants were lacking in that the *Tenancy Act* provided no method as to how bonds should be dealt with by the parties.

The *Tenancy Act* also did not contain provisions that required the landlord to provide statements or that the landlord cannot retain moneys to make good damage caused to the property and the like unless the landlord serves a notice with prescribed information on the tenant.

4.2 The 1991 Review

In mid-1991, the then Government established a working party which was given the task of reviewing the tenancy laws of the Northern Territory.

The working party comprised members of Parliament, members of the real estate industry and government officers drawn from various Departments. The chair of the working party was a Government MLA.

In 1993, a discussion paper prepared by the working party was released for public comment.

The working party prepared a report with numerous recommendations, one of which was the need to establish a central fund to hold bond monies lodged by tenants. This was recognised as necessary to provide a revenue source to fund the expanded tenancy services recommended.

Government accepted most of the working party's recommendations but did not accept the recommendation regarding the central fund to hold bond moneys.

4.3 The 1999 legislation

The *Residential Tenancies Act* was passed in the Legislative Assembly on 14 October 1999 and commenced operation on 1 March 2000.

In his Second Reading Speech, the then Minister, the Hon T Baldwin MLA, said as follows in relation to the central bond holding authority:

“Government carefully considered whether a centralised scheme of holding security deposits should be adopted, but it has decided that the additional administrative costs which would result from the administration of such a scheme would outweigh any benefits tenants would derive from its operation. Government has decided to make a more free market approach to regulation of residential tenancies in this regard. The Bill contains clear and forceful

obligations on landlords in respect of taking, holding and returning security deposits, and it is proposed to rely on the strength of these provisions to protect the interests of tenants.”

4.4 Private Members Bill - Landlord and Tenant (Rental Bonds) Bill 1998

In 1998, the then leader of the Opposition, the Hon Clare Martin MLA, introduced a private members Bill into the Legislative Assembly which was ultimately defeated on 16 February 1999.

The Bill sought to do the following:

- establish a 5 person Board to be called the ‘Rental Bond Board’;
- establish a Rental Bond Account and Rental Bond Interest Account with moneys from the Rental Bond Interest Account to be used for meeting the costs and expenses of administering the Act and also pay for half the costs of administering the *Residential Tenancies Act*;
- provide the Board with broad powers to invest moneys held in the Rental Bond Account and furthermore to enter into joint ventures for residential accommodation;
- provide that all rental bonds held before the inception of the Act would have to be paid to the Board within 1 month of the Act becoming operative;
- after the commencement of the Act, where any residential property landlord receives a bond, he/she must pay it to the Board within 7 days; and
- on request from a lessor or lessee, the Board must pay out the bond to the parties including the relevant interest earned.

4.5 Residential Tenancies Amendment Act 2010

The *Residential Tenancies Amendment Act 2010* commenced on 14 April 2010.

The Amendment Act addressed a number of technical issues with the *Residential Tenancies Act* that had caused difficulties.

The amendments provided that the Commissioner of Tenancies, in determining compensation claims under section 122, must take into account whether the person seeking compensation has consented to the breach of the tenancy agreement or the act that led to the claim. This amendment was aimed at addressing the “Memorandum of Variation” approach to rental increases that is common practice in the Northern Territory. A decision by the Commissioner’s Delegate in *Holdeth Investments Pty Ltd v Ivinson and Halliday*²⁶ put into doubt the validity of this approach to rental increases. Although the Court (on appeal from the decision) upheld the validity of the use of a “Memorandum of Variation”, it was considered appropriate to “put the matter to rest” by amending the Act in this way.

²⁶ [2009] NTMC 016

The *Residential Tenancies Act* was also amended to provide that the Commissioner of Tenancies may pay for a valuation where an “excessive rent” application has been made. This amendment was aimed at removing a sometimes significant financial obstacle for tenants considering pursuing such a claim (and restores what was common administrative practice under the old *Tenancies Act*).

Further amendments clarified that an initial condition report conducted at the commencement of a tenancy would continue to be valid for the whole time a tenant (or at least one of the original tenants) remains in occupation of the premises, even if a new or varied tenancy agreement is created during this period. This specific amendment overcame a technical argument about validity of ongoing condition reports in these circumstances.

4.6 The 2010 Review

Following on from the 2010 amendments, an Issues Paper was developed by the then Department of Justice that focussed on a number of policy and operational issues raised by various stakeholders which indicated there may be a need to consider reform in some areas that went beyond the scope of the technical issues addressed in the amendments.

The Paper was released publically, inviting submissions on the issues raised by stakeholders and any other areas of concern regarding residential tenancies.

The Darwin Community Legal Service, the Central Australian Aboriginal Legal Aid Service and the North Australian Aboriginal Justice Agency in submissions made in response to the Paper all recommended that a centralised bond board should be established. Establishing a board would, in their views, provide a structured and equitable system for the refund of bond moneys, provide greater compliance in the management of bonds and enable ease of access to bond moneys by tenants.

5 Problems with the current system

5.1 General

The Commissioner of Tenancies undertakes, on average, 1000 hearings per year in regard to the *Residential Tenancies Act* of which only a small percentage relate to bond issues. However the Commissioner suggests that, anecdotally, this is very likely due to the fact that tenants generally do not know their rights under the legislation, and as such do not routinely seek return of bond moneys through the Commissioner. In such circumstances, the agent or landlord would generally be obliged to either voluntarily surrender the bond to the tenant, or failing that, the Tenancy Trust Account. It is however not entirely uncommon for the landlord or agent to retain the bond.

Currently, Agents and Landlords also retain the interest on the bonds as an income stream as tenants are not generally aware they can either seek return of the interest earned or the monies are held in accounts that attract very low levels of interest.

The Commissioner of Tenancies is currently not resourced to undertake any form of consumer or general tenant education about their rights and responsibilities under the legislation administered by the Commissioner.

The experience gained in other jurisdictions on the introduction of centralised bond holding authorities has evidenced significant numbers of tenants applying to retrieve the full bond when this was not the case prior to the commencement of a bond board/authority. This has been attributed to the increase in awareness that a bond authority generates through the centralised processes and expanded public education campaigns.

5.2 Return of security deposits

The return of security deposits remains a problem in the current market. The Commissioner of Tenancies reports frequent enquiries from tenants regarding delays in refunding bond monies, noting that it often takes weeks for landlords and agents to return security deposits notwithstanding that the legislation requires bonds to be returned within 7 days of handing over possession of the property.

A significant and related problem is that reasons for delays are not given and it is difficult for the tenant to determine whether there is a claim by an owner for loss or whether the delay arises from poor property management. If the tenant is aware at the outset that the owner intends to retain some or all of the deposit, the tenant can make a claim to the Commissioner.

The prompt return of security deposits is important for all tenants but particularly where tenants move to a new tenancy and need to provide a deposit to a new landlord.

One of the advantages of a well-designed central deposit repository is that deposits can be administratively transferred from one landlord to another.

5.3 Numbers of people making applications

The Commissioner of Tenancies has expressed concern about the low numbers of people accessing the current dispute resolution system.

It appears that many people simply do not apply for dispute resolution. Analysis of complaints statistics from other states and territories supports this concern about low application numbers.

The Commissioner is not resourced to seek to increase awareness of the dispute resolution system by participating in training sessions, liaising with community organisations or undertaking community education programs.

The problem of low application numbers is not fully understood. It appears to be a combination of lack of public awareness and a negative perception.

It could be argued that the problem arises largely from a lack of confidence by tenants in the system, which in turn arises from a perceived imbalance of power.

Community legal service groups suggest that a tenant is more likely to pursue a claim if a third party holds the security deposit. This may partly explain the problem and may result in a feeling that 'it is a waste of time' to pursue a claim because the outcome will not favour the tenant.

As evidenced by submissions to the 2010 Issues Paper, community legal service organisations clearly do not support the current system.

An analysis of bond refund cases determined by the Commissioner since commencement of the *Residential Tenancies Act*, indicates that what is usually in dispute is not the substance of the claim but the quantum. That assessment identified that most disputes arise because some compensation is appropriate but the amount claimed is excessive. Experiences observed in jurisdictions with a centralised bond holding authority has shown that the level of complaints relating to excessive claims against bond monies reduced due to the independent assessment of claims.

5.4 Interstate owners

Another unique factor in the Territory's rental market is the relatively large proportion of landlords who reside outside of the Northern Territory. This factor further contributes to issues surrounding the current administration of rental bonds.

The Commissioner of Tenancies has noted that, notwithstanding the issues discussed above, once a tenant makes an application to the Commissioner, local landlords usually respond within a reasonable time.

That however is not necessarily the outcome in the case of non-local landlords who are not represented by a local agent. The Commissioner's experience is that those landlords more frequently refuse to cooperate with the process and simply ignore requests from the Commissioner.

Unfortunately, the costs of pursuing legal action in other jurisdictions and in some cases outside of Australia are too expensive and certainly greater than the amount of the security deposit. The outcome is that those bond monies are effectively forfeited to the landlord, to the detriment of the tenant. A centralised bond holding authority would eliminate this particular problem.

5.5 Real estate agents

Some real estate agents have also created problems by claiming that the security deposit has been spent effecting repairs or has been otherwise spent in accordance with the direction of the owner. While there may be some argument for such a response in some cases within the bounds of the agency relationship, this approach significantly undermines the effectiveness of the current system.

5.6 Mortgagee sales

It often arises that tenants rent properties from landlords who in turn have mortgages to lending institutions. There have been occasions where some of these mortgagees have defaulted, which has had adverse implications on the ability for a tenant to regain the bond. In these circumstances, it is often impossible to recover the deposit. The defaulting landlord may no longer have possession of the bond (or access to funds to reimburse the bond), or the tenancy has terminated as a result of the process associated with the mortgagee seeking possession.

5.7 Solving current issues

As discussed, the problems are varied and complex. However, it is likely that a concerted education campaign will contribute significantly to increasing public awareness about a dispute resolution system for residential tenancy security deposits. Such a public awareness campaign will need to be funded. Also, if the campaign is successful, there will be an increase in the level of disputes. This would also need to be funded, however current fiscal constraints faced by government limits the ability to adequately resource these activities.

Public perception is a more difficult problem to solve. Clearly, for those people who do not know that a system for dispute resolution exists, public awareness will be effective. However, negative perceptions among those who are aware of the system will be more difficult to solve.

Anecdotal information from community legal service groups suggests that tenants are more likely not to engage in a dispute resolution system if the owner holds the deposit because they do not believe that the process will deliver a fair outcome. Such a perception may arise from a perceived imbalance of power.

Where there is an independent authority to hold the deposit, people are more likely to have confidence in the outcomes of the dispute resolution process and will have a better perception of the system.

Similarly, anecdotal evidence suggests reluctance by tenants to lodge a dispute for fear it will affect any future applications they make for rental properties. In addition to the perception of individual tenants, the level of confidence by community legal service organisations in the existing or an alternate process is critical.

Community legal service organisations have long argued for a bond board, not only because of specific benefits but because the existence of such institutions in other jurisdictions now comprise part of the prevailing Australian rental culture.

With respect to owner and agent problems of non-cooperation, a bond board would eliminate many of the issues. It would also marginally reduce the amount of time to determine each dispute. This is clearly a desirable outcome for tenants. Combined with the need to resolve perceptual issues, there arise a number of advantages for a bond board.

However, the most significant issues are that a public awareness campaign and a consequent increase in disputes will need to be funded. Pooling all of the security deposits in the market and using the interest earned on these funds is the only source of funds that have been identified.

This means that a bond board will need to be established simply to resolve the funding issue. The benefit is that the establishment of such a structure will also assist in resolving the perceptual and owner cooperation issues.

It is also useful to note that the establishment of a rental deposit authority will in time become part of the local culture, which will reduce the need for public awareness campaigns. Conversely, there is likely to be initially a high level of non-compliance by owners. However this will diminish over time.

5.8 Funding a Bond Board

All Australian jurisdictions have rental deposit systems with the exception of the Northern Territory.

In those jurisdictions, considerable funds are generated though the interest received on the money held in trust, which is applied to fund public education programs and dispute resolution systems.

Historically, the only difficulty with such a proposal in the Northern Territory was that the size of the rental housing pool was too small to provide sufficient funds to cover the costs of operating such a system. As discussed in section 7.3 below, that impediment has diminished over time, with the rental housing pool now of a sufficient size to fund a scheme that leveraged off another jurisdiction's existing scheme.

6 Options

6.1 Do nothing

Option 1: Maintain the status quo.

This option would involve proceeding with current law and embarking on a public awareness campaign to better inform participants in the current market. To be effective, expenditure would need to be significant and would need to include radio and television advertising.

However, this option would not resolve emerging issues such as those relating to interstate owners or mortgagee sales. This would require some further legislative change.

Consequently, this option is not recommended.

6.2 Prohibit Security Deposits

Option 2: Legislate to prohibit the collection of security deposits.

One option is to prohibit security deposits altogether. This is an attractive option as it would remove the need for a lodgement and disbursement system as well as the need for dispute resolution processes. However, owners would continue to seek security against loss and damage and would probably reduce this risk through insurance. The costs of such insurance would increase the cost of operating rental property and would most likely be passed onto the tenant, consequently increasing the cost of rent.

This option is not recommended.

6.3 Strengthen the current system

Option 3: Legislate to strengthen the current system.

To make the existing system work better would require further legislative change in addition to increasing public awareness. The most significant problem is establishing a means of recovering security deposits and interest from uncooperative property owners, particularly those living outside of the Northern Territory.

The only effective means of achieving this would be to enable the Commissioner to determine a matter in the absence of the owner and make an ex-gratia award to the tenant where appropriate. The unfunded payment could then be recovered by placing a caveat on the title.

Similarly, legislative change could require an agent to retain a deposit in the absence of agreement by the tenant until such time as the Commissioner determines a dispute. This would ensure that agents did not hide behind the agency relationship as a means of frustrating the existing process.

The advantage of this approach would be that it would not require the establishment of a bond repository or the associated expenditure to operate the repository.

Disputes could be funded in exactly the same way as they are at the present time.

The problem with this approach is that it would not remove perceptions about the existing process or create confidence in the dispute resolution process.

This system would require the enforcement of provisions in the *Residential Tenancies Act* that enable the Commissioner to require all property owners to provide information to tenants outlining their rights under the *Residential Tenancies Act* on both commencement and completion of a residential tenancy agreement.

Strengthening the existing system would not be successful unless market participants were prepared to support the process. This support from either industry or community organisations is unlikely and consequently this option is not considered to be viable.

6.4 Establish a Residential Deposit Authority

Option 4: Legislate for the establishment of a central bond holding scheme.
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The establishment of a residential deposit authority appears to be the only option which will resolve most of the current issues. It will provide the best means of improving tenant confidence in the process, particularly as it is the option most likely to be supported by community organisations.

Secondary advantages include the pooling of money to fund dispute resolution and public awareness programs. Establishment of a residential deposit authority will also enable the collection of statistics on the private rental market that have previously been unavailable.

This data will be valuable in a number of contexts, including housing policy development and inter-jurisdictional comparisons.

This is the recommended option and is further discussed in this Paper.

7 The Legislative Proposal

7.1 Proposal

It is proposed to legislate to create a Northern Territory Centralised Residential Tenancy Bond Authority which would hold all bond monies for residential properties throughout the Northern Territory.

It would also hold unclaimed bond monies which are currently held by the Commissioner of Tenancies in a Tenancy Trust Account. As at January 2015, the trust account held unclaimed bonds totalling \$298,590.18.

7.2 Objectives of the Legislation

The objectives of the legislation should be:

- (1) to increase tenant and owner awareness of existing dispute resolution processes for residential tenancy security deposits;
- (2) to obtain equity and fairness in landlord and tenant relationships;
- (3) to improve tenant and owner confidence in existing dispute resolution processes; and
- (4) to identify and access funding for increased public awareness and dispute resolution activity.

The legislation could:

- (1) establish a Rental Deposit Authority (RDA), under the authority of the Commissioner of Tenancies to receive all security deposits on behalf of property owners;
- (2) prohibit the direct payment of security deposits to owners and agents in connection with residential tenancy agreements;
- (3) create a statutory obligation for the RDA to educate the public about the obligations of the *Residential Tenancies Act*;
- (4) create relevant statutory offences where owners fail to comply with the RDA requirements or receive security deposits;
- (5) provide for all monies held by the RDA to be placed in an approved interest bearing account, with all surplus funds to be invested with the Northern Territory Treasury Corporation or another entity approved by Government;
- (6) require any funds surplus to operating requirements to be returned to the Central Holding Authority; and
- (7) provide that the RDA can be managed in-house or delivered through an outsourced model via another jurisdiction's scheme.

7.3 Delivering the service

7.3.1 Costs

As part of the background work undertaken to inform development of this Issues Paper, a preliminary assessment of the potential costs of a Northern Territory Centralised Residential Tenancy Bond Authority, its likely bond holdings and potential income stream was undertaken by the Department of Treasury and Finance.

The Department of Treasury and Finance assessment identified and compared two options for management of the Authority:

- the Territory self-manages the bond services; or
- partnering with another jurisdiction that has an existing system for outsourcing the bond management services to a private sector registry service provider.

In undertaking the assessment, it was determined, based on a review of other jurisdictions' schemes, that the Tasmanian model be used as a base due to Tasmania's similar demographic characteristics to the Territory (small, regional population bases), permitting a realistic comparator on cost and scale, which would not otherwise be possible against larger state schemes. The level of technological integration applied to the Tasmanian scheme was also identified as being best suited to the Territory's needs. The Tasmanian Bond Authority was consulted during the assessment to further inform the analysis.

The analysis validated the selection of the Tasmanian model as a comparator, with outcomes modelled for the Territory expected to be similar to those experienced in Tasmania. The assessment indicated that:

- an in-house managed model would likely run at a loss over an extended period; whereas
- from inception, partnership with another jurisdiction would likely return a modest surplus from operations.

Details on the Tasmanian scheme are provided in Attachment A.

8 Nature of the restrictions on business

The proposal to establish a residential deposit authority will not directly impact on competition in the market.

There is no identifiable market for the provision or collection of security deposits and consequently no business activity will cease as a result of the establishment of such an authority.

A residential deposit authority will displace the existing requirements for the real estate industry where security deposits are placed in statutory trust accounts in accordance with the *Agents Licensing Act*.

The principal market that is relevant for this discussion is the market for rental properties. Owners reduce the risks that exist in this market by requesting a security deposit from tenants as a guarantee against the performance of certain obligations. The proposal to establish a residential deposit authority will not impact upon this practice.

Another form of protection owners frequently take out is that of insurance. Insurance can be obtained against fire and building damage and against rental loss, court costs and malicious damage. Most of these policies have an excess for general building damage and for rental loss and malicious damage. These policies generally pay out the amount of loss in excess of that recovered by the legal amount of security deposit that can be obtained. The establishment of a residential deposit authority would not influence a landlord's ability or choice to consider insurance coverage, nor would it influence the insurance market generally, or insurance premiums specifically.

The proposal will mean that only Government will be involved in the collection and disbursement of security deposits. This will establish an effective monopoly by statutory force. However, this will not displace an existing market as the organised activity is not possible without statutory authority.

8.1 Impact on Business

8.1.1 Costs

There will be minimal cost impact on business as a result of establishing a residential deposit authority.

The net impact to private owners under the current unregulated market is however difficult to estimate. For example, private owners will no longer be able to obtain incidental benefits that accrue from holding a security deposit.

Private owners currently manage security deposits in a number of ways and therefore obtain varying benefits. Some owners may deposit the bond into a bank account and retain the interest. Other owners might hold the bond in cash at their residence or even spend the money. In this case they are using the money as an interest free loan. The net impact to owners in this case depends on how that money would have been sourced if the owner did not have access to the security deposit.

However, when considering these potential costs, it must be accepted that the security deposit and interest belongs to the tenant. Responsible property owners would keep the money separate from their own financial affairs and thus would not be impacted by the introduction of a residential bond holding authority.

Real estate agents currently place security deposits in trust accounts, and the interest earned on these accounts is retained by the agents. This will mean agents will lose the benefit of retaining interest on bond moneys held in trust where that interest was retained rather than refunded under the *Residential Tenancies Act*. Tenants will also lose the benefit of that interest as it will instead be applied to fund the scheme.

There will be some transaction costs associated with the proposed system, predominantly in respect to obtaining and completing the documents required to lodge and claim a bond. As the forms will be completed at the points in the process where bond money is currently exchanged, the impost would be marginal. Changes to the legal requirements and procedures may also necessitate modification of staff and organisational practices, however any such modification (including any training requirements) is expected to be minimal.

As noted above, the introduction of a central bond scheme in other jurisdictions saw an increase in the number of bond release applications by tenants. On the basis of that experience, there is a possibility that there will also be some additional costs to tenants and landlords as a result of an initial increase in the number of disputes under the scheme. While this is not quantifiable, it is anticipated that, should an increase in disputes eventuate, this factor will be a short-term consideration as landlords, agents and tenants adjust practices to operate within the scheme.

In addition, there will be a cost to Government in developing and implementing new legislation. There will also be ongoing costs in managing the collection and disbursement system as well as those costs associated with ensuring public awareness.

As noted in section 7.3.1, an in-house delivery model (i.e. the scheme is established in the Northern Territory and operated by the Commissioner of Tenancies) is unlikely to be self-supporting. However an outsourced service delivery model (i.e. one that is operated on the Territory's behalf by one of the other jurisdictions – such as Tasmania) is likely to be self-sufficient.

8.1.2 Benefits

The establishment of a central residential bond holding authority will standardise the collection, administration and distribution of residential bond money.

A significant benefit of the proposed system is the more equitable distribution of security deposit monies. If the establishment of a residential bond holding authority delivers the anticipated increase in security deposit applications, this will result in a significant increase in the total amount of funds disbursed back to tenants.

The primary (but difficult to quantify) benefit will be increased awareness and confidence that a standard system of bond processing delivers. Public awareness of the rights and responsibilities surrounding bond money will mean that more people will have confidence in the dispute resolution processes when they believe that

deposits have been retained unfairly. It will also mean that landlords and agents will be more circumspect over seeking to retain deposits without challenge.

Secondary benefits include the ability to apply earnings from a centralised fund to increase the community's knowledge about residential tenancy law and the operation of the *Residential Tenancies Act*, assisting the Commissioner to disseminate information in a way that is not currently possible. The establishment of a central authority would also facilitate the generation of reliable statistics, enabling government and industry to undertake meaningful analysis of the Territory's rental market.

The establishment of a bond holding authority would also reduce administrative costs to landlords and agents through removing the necessity for operating and managing security deposit trust accounts.

Another area of benefit found in Tasmania was that a large number of private landlords elected to rent their properties through property agents following introduction of the Tasmanian Bond Authority. The Tasmanian Authority attributes this to landlord desire to comply with the scheme, and ensuring that the paperwork was completed properly so that they did not lose their ability to seek distribution of bonds where entitled.

9 Greatest Net Benefit/Least Net Cost Alternative

The foregoing dialogue suggests that while a range of options are possible, only the establishment of a centralised residential bond holding scheme has the potential to resolve the policy issues and deliver the required public benefit.

As outlined above, the current rental bond arrangements result in imposts on both tenants and landlords/agents. For tenants, there is the issue over the prospect of return of the bond. For landlords/agents, there are costs associated with managing the bond money on trust for the tenant. The establishment of a centralised scheme would remove those imposts.

The challenge is to create a process that is easy to use for both tenants and landlords and delivers the maximum benefit for the least cost. Consequently, there is little viable choice but to establish a centralised residential bond holding scheme as a means of solving relevant problems in the existing market.

As previously mentioned, the least cost and least risk method for doing this is to enter into a partnership with another jurisdiction to deliver the centralised residential bond holding scheme via an established State or Territory operated scheme.

Attachment A

1 The Tasmanian Model

1.1 Introduction

The Rental Deposit Authority (RDA) in Tasmania is supported by an innovative arrangement with a US company based in Bangalore India. The RDA, which was established in July 2009, operates via an internet connection to a database that exists in Melbourne and is managed on a daily basis by iGate staff from within Australia. There is oversight and management of the database from Bangalore and there is regular dialogue between the RDA and the Australian and Indian staff from iGate.

Data entry for both lodgement and claims are managed by iGate through optical character recognition and a fax server. Matching of signatures between lodgement and claims is done by staff in Bangalore.

RDA staff in Hobart follow up errors (such as missing signatures, missing data, conflicting data and incorrect financial information) and manage a reconciliation process for financial transactions with assistance and reports from iGate.

iGate services are provided on a fee per transaction basis. iGate charge a standard amount for a defined number of transactions and an additional fee for each transaction that exceeds this ceiling. There is currently a 5 year contract for iGate to host and manage the database and provide a range of defined services. Any development work for enhancements to the database is done on a fee for service basis. Most of this development work is done by staff in Bangalore.

This arrangement means the Tasmanian Department of Justice does not own any hardware (other than a scanner) and does not support any software to run the operation of the RDA. The advantages of this arrangement is that the risks of managing this system are transferred via contract to iGate and the number of staff that need to be employed by Government is reduced. The RDA has 3 officers in Hobart.

The successful operation of the RDA relies on a strong relationship between the RDA and iGate. As iGate specialise in this type of arrangement, their customer services and responsiveness are excellent. In general terms, the relationship is a resounding success.

1.2 Rental Deposit Authority

The RDA is a statutory body established under the Tasmanian *Residential Tenancy Act 1997* to act as a neutral repository of rental bonds paid by tenants as security for the performance of residential tenancy agreements.

The RDA collects bonds, holds the bonds until the end of the tenancy and disburses the bond according to the agreement of tenants and property owners or in accordance with the direction of the Residential Tenancy Commissioner or a magistrate.

The RDA currently holds \$34.4M in rental bonds, which represents a total of 35,549 Bonds.

The RDA collected 19,056 rental bonds in the 2013-14 financial year and paid out 15,808 rental bonds.

1.3 Lodgement of rental bonds

The Tasmanian *Residential Tenancy Act 1997*, unlike the system in most other jurisdictions, prohibits the receipt of bond money by a property owner. Tenants must pay bond monies directly to the RDA, or to a real estate agent who is registered specifically for the receipt of bond monies. Service Tasmania forwards the lodgement forms to the RDA and the bonds are electronically transferred to the RDA Trust Fund. Real estate agents are required by law to pay a rental bond to the RDA within three business days of receiving the bond from the tenant. Where real estate agents are also registered agents of the RDA, they are permitted by contract to pay bond monies on a weekly basis.

1.4 Storage and Management of data

Relevant data about each rental bond deposited with the RDA is contained within the physical lodgement form. All lodgement forms are sent physically to the RDA which is located within Consumer Affairs and Fair Trading at 15 Murray St. All bond lodgement forms are scanned and the images transferred to a database operated by a company called iGate. The forms are designed to facilitate optical character recognition and the automatic entry of data into the RDA database. The RDA deals with any data errors/exception or missing data. The database is managed by iGate and access to data is obtained via the internet. iGate host, manage and backup the database. The iGate/RDA Server is located in Melbourne.

1.5 Claims

All claims (requests for return of the rental bond) are sent by either the claimant or a real estate agent to an iGate fax server located in Melbourne. The data on the claim form is entered into the RDA/iGate database. A claim form is to be signed by all parties. The parties may agree to a disbursement of the bond or may disagree. Where there is a disagreement or no agreement, the matter is referred to the Residential Tenancy Commissioner. Disbursement is made in accordance with the decision of the Commissioner. There is a right of appeal against the Commissioner's decision to a magistrate and final payment is made in accordance with the magistrates' decision.

Payment is made according to agreement or decision and on the verification of signatures. Signatures are matched by visual verification by staff in Bangalore. Where there is a clear match, payment is authorised on this basis. Where there is any doubt about the validity of the claim, the claim is referred back to the RDA in Hobart for review. All verified and approved claims are submitted to the finance section of Tasmania's Department of Justice in Hobart for processing and deposit electronically into the recipients' bank account. These instructions are transferred overnight and payments occur each business day.

1.6 RDA functionality

The iGate/RDA database provides for searches of existing rental bonds and is configured to enable Tasmania's Office of Consumer Affairs and Fair Trading call centre to answer telephone inquiries from tenants and owners about the progress of bond payments. Follow up and alteration to fix errors and omissions in bond records is managed from the RDA in Hobart.

The day to day management of the database is undertaken by iGate who have a centre in Ballarat. iGate also manage the Victorian Rental Bond Authority however the processes are different and more reliant on paper processes. There is no facility for optical character recognition in the Victorian system which relies on manual data entry. Also, in Victoria, iGate manage the funds and process payments. The Fund in Victoria has a current balance of \$770 million. In Tasmania, all funds are managed within Government.

The verification of signatures and the development of database are managed from Bangalore in India. Bangalore oversees the operation and management of the RDA database.

1.7 iGate

iGate is an American Company, registered in Chicago but based in Bangalore India. The company has a small presence in Australia but operates in Canada, the UK, the US and India. iGate specialise in providing a package of business activities which include database management and back office functions.