

RETIREMENT VILLAGE ALERT SEPTEMBER 2014

CAPITAL MAINTENANCE AND REPLACEMENT - TRIBUNAL GIVES PRACTICAL GUIDANCE

In the recent case of *Alloura Waters Retirement Village Residents Committee v Living Choice Australia Pty Ltd* [2014] NSWCATCD 68 the residents' committee of Alloura Waters Retirement Village (**Village**) brought an action against the operator, Living Choice Australia Pty Ltd (**Operator**) seeking an order that certain recurrent charges be refunded to the residents on the basis that the operator had expended them otherwise than in accordance with the *Retirement Villages Act 1999* (NSW) (**Act**).

The findings of the NSW Civil and Administrative Tribunal (**Tribunal**) include a detailed discussion of:

- what capital maintenance means under the Act;
- when expenditure will be in accordance with the budget; and
- when an operator will be found to be obstructing the residents' committee,

making it key reading for those involved in retirement village management. The findings of the Tribunal on the key issues in the case are summarised below.

Capital maintenance (and repair) v capital replacement

A key claim of the residents' committee was that certain expenditure had been incorrectly characterised as capital maintenance (rather than capital replacement) by the Operator and funded from recurrent charges.

Under the Act the operator must maintain the items of capital for which it is responsible in a reasonable condition (s93). If it is not practicable to undertake maintenance, the operator may replace the item. However, only capital maintenance and not capital replacement may be funded from recurrent charges.

The Tribunal noted that the meaning of capital maintenance in the Act, being "*works carried out for the purpose of repairing or maintaining an item of capital...*" includes both the concepts of 'maintenance' and 'repair'. As such, when considering whether expenditure was properly capital maintenance, the Tribunal had to consider whether it fell into either 'maintenance' or 'repair'. The Tribunal considered that:

- A 'Repair', "*...replaces or corrects something or corrects something that is already there and has become worn out and dilapidated by ordinary wear and tear, by accidental or deliberate damage, or by the operation of natural causes. A minor incidental degree of improvement, addition or alteration may be done to property and still constitute a repair*".

- ‘Maintenance’, “... is work done to keep an item of equipment functioning efficiently or to extend its economic life by enhancing or improving it. Ordinarily ‘maintenance’ involves repair work which is performed to prevent defects damage or deterioration; but ... may take on a wider meaning that includes repairing as well as other operations which are apt to enhance an item of capital. So long as the work done does not substantially improve the item of capital beyond its original condition it is to be treated as a capital maintenance item...”

The Tribunal then considered each disputed item of expenditure by reference to the above principles. The Tribunal rejected a contention that the Operator needed to justify the expenditure as being in accordance with the Act and found that the onus is on the residents’ committee to lead evidence showing why the expenditure is incorrectly characterised. The expenditure considered by the Tribunal was broad ranging and included:

- mop, mop covers and crockery – the Tribunal found that these items were not items of capital, but rather consumables used in the ordinary course of business and therefore their replacement was not ‘capital replacement’;
- fixing digital television aerials involving identifying the causes of faulty equipment and repairing that equipment – the Tribunal found that this was capital maintenance;
- replacement of 33 metres of a total of 236 metres of guttering where the replacement guttering was deeper and squarer – the Tribunal found that the new guttering was an improvement and properly characterised as capital replacement; and
- air conditioning control unit costs – the Tribunal found that this expenditure was capital maintenance as it related to responding to maintenance requests initiated by residents or staff members.

Expenditure not in accordance with the village budget

The residents’ committee also argued that the Operator had expended funds otherwise than in accordance with the village budget, in contravention of the Act.

Under the Act, the operator must not expend recurrent charges otherwise than in accordance with the approved annual budget, subject to minor variations (s116(3)). The residents’ committee argued that s 116 requires that expenditure correspond line by line to the approved budget, which had not been the case at the Village.

However, the Tribunal found that the Act did not place such restrictions on the management of retirement villages and that s 116(3A) of the Act allows variation between the budget and actual expenditure provided that the level of services at the village is not reduced or total expenditure provided for by the approved budget is not exceeded. As there was no evidence that this was the case, the Tribunal held that the residents’ committee failed to make out this claim. That is, the Tribunal considered that the Operator did not have to follow the budget line by line to comply with the Act – a significant win for operators.

Residents’ committee obstruction

There was an allegation that the Operator had obstructed the residents’ committee in its work by failing to deal with requests for information quickly enough or by providing inadequate information when it did respond. The

Tribunal held that this did not amount to obstruction of the committee's functions by the Operator. To the contrary, the Tribunal found that the Operator supported the functions of the residents' committee by responding to its requests for information.

Whether expenditure is capital maintenance or capital replacement will often turn on the particular circumstances of the expenditure. However, the detailed discussion in this case provides useful guidance on the way that the Tribunal will approach an allegation by a residents' committee that expenditure was otherwise than in accordance with the Act.

APPROACHING LAPSE OF REGULATIONS

The *Retirement Villages Regulation 2009* (NSW) (**Regulations**) are due to lapse on 1 September 2015. The Government may choose to let the Regulations lapse, postpone the lapse by up to a year, remake the Regulations in the same form or remake them with amendments.

If the Regulations are remade there will be a compulsory period of public consultation of at least 28 days.

The review of the Regulations presents an opportunity for the Government to clarify the uncertainty amongst operators and residents regarding what constitutes capital maintenance and capital replacement under the Act, as highlighted in *Alloura Waters Retirement Village Residents Committee v Living Choice Australia Pty Ltd*.

Whether the Government takes the opportunity to inject certainty into the Regulations based on the comments of the Tribunal in *Alloura Waters* remains to be seen.

We will keep you updated on the regulation review process.

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