PHARMACY OVERVIEW

COMMUNITY PHARMACY PROFILE

Community pharmacies are captured within the Australian and New Zealand Standard Industrial Classification (ANZSIC) classification of ‘retail trade’, under Class 4271 ‘Pharmaceutical, Cosmetic and Toiletry Goods Retailing’.

There are approximately 5,723 community pharmacies in Australia (Department of Human Services)\(^1\). The sector employed approximately 60,000 people (20,000 registered pharmacists and 40,000 pharmacy assistants) in 2016–17.

Community pharmacies continue to play a pivotal role in providing primary healthcare and delivering a wide range of services including dispensing prescriptions; distributing pharmacy only and pharmacist only medicines and over-the-counter products; medication management; advice on minor ailments; and preventive care services. Ultimately, community pharmacies operate to improve the timely access and quality use of medicines in Australia.

At the same time, community pharmacy is practised in a commercial environment – and like other small businesses, the success and viability of the community pharmacy sector depends on the financial performance of these small businesses in the context of the broader pharmaceutical supply chain.

Community pharmacists own and operate their businesses – forming an integral part of local communities and contributing to local employment and economic activity.

The average revenue per pharmacy is $2.81 million and 66% of revenue is derived from the sale of prescription medicines. The other 34% includes pharmacy professional services, pharmacy only medicines and over-the-counter products. The gross margin (sales less cost of goods sold) is just over $1 million for the average pharmacy and average annual net profit equates to nearly $110,000\(^2\).

Rural pharmacies represent 16% of the total community pharmacies and there is approximately one (1) pharmacy for every 4,236 Australians. The accessibility of community pharmacy is a strong factor underpinning the high regard in which community pharmacy is held. On average, community pharmacies are open 62 hours a week, and are open for an average of 10 hours a day during the week\(^3\).

After cost of goods sold and wages/salaries, rent is the next largest expense for many pharmacies. For the average pharmacy dispensing 57,442 prescriptions, trading 62 hours per week and with a size of 239 square metres, rent expenses are approximately 6% of sales.

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1. PBS Expenditure and Prescriptions 2017-18, Department of Health
2. Guild Digest 2016
3. IBISWorld Industry Report G4271a Pharmacies in Australia 2017
VALUE OF PHARMACY TO LANDLORDS

In any shopping precinct the selection of retail businesses and how they complement each other will determine the effectiveness of the tenancy mix. Whether located in a large shopping centre or a small strip, community pharmacies are an essential component of any effective tenancy mix and are ultimately high value tenants.

The essential goods and services offered by pharmacies as valued health care providers ensure pharmacies regularly draw customers, generating foot traffic in any retail precinct.

The primary product offerings are prescription-only medicines and over-the-counter controlled ‘pharmacist only’ medicines. Provision of ‘pharmacist only medicines’ requires personal counselling by a pharmacist, thereby ensuring a continued stream of consumers, the vast majority of which (94%) will be served/delivered through a community pharmacy. Community pharmacies also offer health care items, cosmetics, toiletries and other items.

Pharmacies draw high foot traffic and repeat visits to retail centres where they are located. An average community pharmacy will dispense 57,442 prescriptions annually, approximately 13 scripts for every person in Australia.

As the only premises permitted to dispense prescription-only and other restricted medicines, a community pharmacy is essential for retail locations to provide a complete service to customers. High prescription levels range across the demographic spectrum and for those with chronic conditions, visiting a pharmacy is part of their essential shopping routine.

Pharmacists enjoy a highly trusted relationship with their customers. According to a survey conducted by the Institute for Choice for the Pharmacy Guild of Australia:

- 89% of consumers trust their local pharmacist either very highly or completely
- 64% of consumers support the principle that professionals should own the business they work in
- Community pharmacies have a clear advantage over supermarkets in terms of trust and quality of service
- Consumers trust their local pharmacist to deliver the medicines they need and have a level of trust in community pharmacy that greatly exceeds their trust in other potential sources of supply.

In absolute terms, the overwhelming majority of survey respondents place a high degree of trust in the ability of their local pharmacy to provide the best service and advice.

PROFESSIONAL HEALTH SERVICES

Based on their position of trust in the community and the skills that pharmacists possess as health professionals, community pharmacies are increasingly operating as primary health care outlets.

Pharmacies also operate as a primary health destination which customers will attend for immediate medical advice and health services. Professional services include blood pressure tests, home medication reviews, bowel cancer screenings, weight management programs, ‘Quit’ smoking support, baby and maternal health services, disease screening, medication management and vaccinations.

STABLE, LOW-RISK TENANTS

Historically community pharmacies have held a strong reputation for having a very low risk of failure, with income generated from government payments and consistent demand for pharmacy products and services.

Pharmacies have significant goodwill attached to their business. With the importance of this goodwill to business performance, and the high cost of a new fit-out, pharmacies are traditionally unlikely to relocate premises but instead seek long-term leases, and are thus stable long term tenants.

4 IBISWorld Industry Report G4271a Pharmacies in Australia 2017
5 Approximately 184 scripts per day based upon a 6 day operating cycle
6 Guild Digest 2016
8 Increasing the provision of such professional services is being supported by the Australian Government, most recently in the 2017–18 Budget, however providing these services is not without cost.
EXCLUSIVE LOCATION REGULATIONS

The current statutory framework for community pharmacies requires that pharmacies be owned and operated by pharmacists, and imposes certain limitations on the location of new pharmacies or the relocation of existing Pharmaceutical Benefits Scheme (PBS) approved pharmacies.

Legislating the supply of pharmaceutical benefits at particular premises will provide an additional source of stability for pharmacy tenants. The Australian Government has passed legislation cementing the ‘location rules’ by amending the relevant sections of the National Health Act 1953.

RENTAL / LEASING

DEFINITION & REGULATORY CONSIDERATIONS

A retail commercial lease, also known as a retail lease, is a legally binding contract that spells out the rights and responsibilities of a tenant and landlord in respect to retail premises. Retail leasing legislation is State-based, which means that the definition of a retail lease differs in each State and Territory. As a general rule, if the property being leased has a shop front, is in a shopping centre and/or is mainly used for selling goods or services to the public then the lease of such a property will most likely be considered to be a retail lease.

As far as rent is concerned, ordinary commercial leases can be prepared on a number of bases. For example, rent could be calculated as follows:

- Base rent, no outgoings
- Base rent, plus outgoings
- Base rent, plus a percentage of sales
- Rent review as market review, fixed percentage, based on CPI measure.

The bargaining positions of the landlord and tenant, including each of their size, demand for premises and strength of the market, could determine the rental terms of the commercial lease.

WHAT IS A REGISTERED LEASE?

A registered lease is a lease that is registered on the title of a property. In the majority of States, a lease which is for a period of three (3) years or longer must be registered.

A registered lease provides a tenant with additional property rights compared to an unregistered lease.

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9 Budget Paper No.2, Page 115
10 % of sales may not be compliant in some state and territory legislation for pharmacy ownership (refer to turnover reporting guidelines).
WHAT TO DO BEFORE YOU SIGN A RETAIL LEASE

The landlord is required by law to give the tenant a draft copy of the lease before it is signed. In some States, the landlord is also required to provide disclosure statements and copies of other documents as specified in the relevant legislation.

Before you sign a lease you should always:

- Take time to review the clauses and terms of the lease
- Discuss any contentious matters with the landlord
- Do not make the mistake and assume the leasing terms cannot be negotiated
- Read any relevant legislation
- Talk to someone from your small business association, fair trading office or a small business lawyer
- Talk to a leasing lawyer, if necessary.

PURPOSES AND RESTRICTIONS CLAUSES

You should check the lease to see if there are clauses which restrict your business activity, such as:

- Does the lease restrict certain types of business activity?
- Does it factor in any potential changes which may occur?
- Does it prohibit you from offering certain services?
- How does the lease provide for any ‘permitted use’ changes during the lease term?

RENT REVIEW CLAUSES

You should check to see what the lease says about rent and changes to the rent. The rent clause or clauses may include changes as a result of increases in CPI, market rent reviews and annual increases.

INSURANCE

The lease should spell out whether or not the landlord insures the property and the tenant’s insurance obligations. In any event, you should consider taking out insurance. If you are unsure about your insurance options you should speak to an insurance broker or business lawyer.

WHEN DOES A RETAIL LEASE START?

A retail lease generally starts on the date specified in the lease document, after it is signed by both the tenant and landlord. It may also start before the formal signing of the lease if the tenant takes possession of the premises before signing the lease.

THE LENGTH OF THE LEASE

One of the essential things you should work out from the start is the term of the lease, including whether or not there is an option to renew at the end of the lease and if so, on what terms or can the lease be less than the minimum as required in some States/Territories.

Commercial leases are generally entered into for a period of 3 to 25 years, which includes an initial term and options for the tenant to renew the lease. For example, a 25 year lease would usually be for an initial term of 5 to 10 years followed by successive options of 5 to 10 years each.

COSTS IN RETAIL LEASES

You need to clarify what the lease says about who is responsible for costs, such as:

- Costs of preparing the lease
- Costs of changing the lease
- Signage, fixtures and fittings
- Stamp duty
- Legal fees
- Promotion and advertising
- Cleaning
- Outgoings
- Wear and tear
- Make good (i.e. at the end of the lease returning the property to the condition it was in at the start of the lease)
- GST.
WHAT STATE IS YOUR BUSINESS LOCATED?

There is no national legislation to cover rental/leasing arrangements. Each State/Territory has its own respective legislation (as at November 2017) which is indicated below:

<table>
<thead>
<tr>
<th>STATE</th>
<th>LEGISLATION</th>
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<tbody>
<tr>
<td>VIC</td>
<td>Retail Leases Act 2003</td>
</tr>
<tr>
<td>NSW</td>
<td>Retail Leases Act 1994</td>
</tr>
<tr>
<td>SA</td>
<td>Retail &amp; Commercial Leases Act 1995</td>
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<tr>
<td>WA</td>
<td>Commercial Tenancy (Retail Shops) Agreement Act 1985</td>
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<tr>
<td>ACT</td>
<td>Leases (Commercial and Retail) Act 2001</td>
</tr>
<tr>
<td>QLD</td>
<td>Retail Shop Leases Act 1994</td>
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<tr>
<td>NT</td>
<td>Business Tenancies (Fair Dealings) Act 2003</td>
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<tr>
<td>TAS</td>
<td>Fair Trading (Code of Practice for Retail Tenancies) Regulations 1998</td>
</tr>
</tbody>
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WHAT IS AN UNFAIR CONTRACT TERM UNDER MY LEASE?

Tenants should also familiarise themselves with the unfair contract terms legislation that came into effect on 12 November 2016. These provisions help to protect small businesses (i.e. 20 employees or less).

If a term would cause a significant imbalance between the rights of the landlord and the tenant, it may be considered unfair. For instance, unfair terms may include clauses that:

- Restrict a tenant’s right to claim compensation from the landlord
- Appoint the landlord as the tenant’s power of attorney if they default on the lease; or
- Terms that allow the landlord to grant an easement over the premises.

More information is available from:
- Australian Consumer and Competition Commission (ACCC)
- Australian Small Business and Family Enterprise Ombudsman (ASBFEO); or
- Small Business Commissioner in each State or Territory.
RENTAL / LEASING COSTS

WHAT PERCENTAGE OF RENT SHOULD YOU PAY ACCORDING TO YOUR BUSINESS’ GROSS INCOME?

Building rent is a common fixed cost for businesses. Like other overhead costs, it is important to invest a reasonable amount in rent to give yourself a chance to earn bottom-line profit. Though specific percentages vary by industry, rent as a percentage of gross income is a metric often used to keep rental costs in check. In general, businesses with smaller gross profit margins need to maintain lower rent percentages to achieve net profit.

RATIO OF ANNUAL RENT TO ANNUAL SALES

The ratio of a business’ annual gross rent to its gross sales receipts is referred to as the company’s occupancy cost ratio. The figure expresses the percentage of the company’s revenue spent on leasing the business premises each year. Occupancy cost ratios need to be considered as part of a bigger picture that includes other expenses, such as staffing, taxes and debt repayments.

OCCUPANCY COST RATIO

A measure of the retail business overall performance is the Occupancy Cost Ratio (OCR = gross rent as a percentage of Retail Sales) and the productivity measure of turnover per square metre. (Noting that retail sales and turnover refers to front of shop sales – excluding dispensary turnover/income).

Calculating the gross occupancy cost ratio of a premises requires dividing the total annual gross rent by gross sales. Gross occupancy = total annual gross rent / annual gross sales.

For example:
If a business pays:
• Rent per year of $24,000
• Annual sales of $125,000
• $24,000 as percentage of $125,000
• The result is 19.2%, which means the business spends 19.2% of its total receipts on rent.

The object of this ratio is to identify the performance of the physical real estate, the net lettable area (NLA measured in square metres) under lease. It should be noted here that to effectively measure the true performance in terms of location, size, access and retail market opportunity, only retail (front of shop sales) should be considered.

This ratio should be evaluated against industry benchmarks to clearly identify the size (m²) requirements of a particular retail business, as one of the key areas of excessive rental and OCR is a premises that is too large for the actual business volumes.

IDEAL LEVEL

There is no ideal level for a business’ occupancy costs because a business’ bottom line is influenced by a number of other factors. If a business’ occupancy costs percentage is in the high teens and it struggles to make a profit, it should consider looking at other premises or discussing options with the landlord. If a business doesn’t do well despite the fact it pays low occupancy costs, it may consider moving into more expensive premises that will attract more customers.

LOW OCCUPANCY COSTS

A business that has low occupancy costs is better placed to withstand economic volatility and rising supplier prices and staffing costs. A low rent-to-sales ratio, however, isn’t necessarily a sign that a business pays a low rent to its landlord. Although prime retail space in malls and on busy shopping streets is expensive when compared to smaller premises on the outskirts of towns, the increased footfall and higher level of passing customers can more than compensate for more costly rent.

HIGH OCCUPANCY COSTS

If a business’ occupancy costs are too high, then asking the landlord for a reduction in rent is an option. Looking into the landlord’s circumstances before making an approach is wise, though, if the landlord has other unoccupied retail space and the business can obtain a less expensive deal elsewhere, then the business’ representatives could state that the business will have to move unless the rent is cut. Lease reductions can be anywhere from 5% to 50% when the retail sector suffers a significant downturn.

By analysing the ratios of OCR and turnover/m² and comparing with industry benchmarks, more efficient use of real estate under lease and better decision making and negotiating of commercial lease terms can be achieved.
SETTING PHARMACY RENTS

Negotiation of leasing agreements need to be undertaken fairly, with understanding of the particular circumstances in which community pharmacies operate.

ESTABLISHMENT COSTS

Pharmacies require a large amount of capital to establish, through purchase of approval number, store fit-out and establishment of a client base.

Fit-out cost is an expense which must be considered as part of the occupancy costs of a pharmacy.

Pharmacy fit-out costs can range between $1,250 and $1,750 per square metre. Based on this sample, the median pharmacy with a size of 214.5 square metres could invest between $267,500 and $374,500 on a shop refit. In a community setting (i.e. strip shopping centre), it is expected that the pharmacy could be required to be updated approximately once every 10 years, this is dependent upon lease management including terms and conditions.

In major regional shopping centres, the median pharmacy size is approximately 352 square metres and a pharmacy could typically invest between $440,000 and $616,000. It is not unusual for larger pharmacies to spend in excess of $1 million on shop fit-outs. However, shopping centres may require the fit-out to be updated every 3 to 5 years as part of leasing arrangements.

These costs can be significant with investment required to regularly be made in fit-outs to meet landlord specifications. Whilst fit-out costs are not part of rent, they can be largely driven by landlords and add to the total occupancy costs of pharmacy businesses.

PHARMACY – A DISTINCT CASE

When negotiating leasing arrangements, Guild members should satisfy themselves that any comparative occupancy cost measures provided or referenced by the landlord or his or her agent directly reflect pharmacy only benchmarks.

Shopping Centre Classifications Sales Category

Under Shopping Centre Council of Australia (SCCA) guidelines, community pharmacies are included under the general retail sales group category. This category also includes other retail channels such as giftware, cosmetics, discount variety stores, florist shops, pet shops, toy stores and miscellaneous retail outlets.

The average net lettable area of pharmacy stores is also substantially larger than most specialty stores.

In the collation of sales and rental data by landlords for the purposes of rent setting, pharmacy is collated with cosmetics retailers. This classification skews the averages and has flow on impact for the application of this data when negotiating rents, as stores in the cosmetics channel usually lease smaller premises and pay higher per square metre rates.

SHOPPING CENTRE PHARMACIES

Many pharmacies are located within shopping centres. These pharmacies may be subject to guidelines which affect the types of information requested and thereby lease negotiations.

Sales Reporting Guidelines

In November 2018 the Pharmacy Guild of Australia, Australian Retailers Association, National Retailers Association along with the Shopping Centre Council of Australia endorsed and became signatories to The Reporting of Sales and Occupancy Costs-Retail Industry Code of Practice.

The Code took effect on the 1st January 2019 with a 6 month implementation period to the 30th June 2019. From the 1st July 2019 Landlords will have a mutual obligation where Lessee’s are contractually required to report sales under a Retail Lease in return share data back with Lessees including sales and traffic and importantly prescribe how they treat this data (particularly when applying GST uplift and retail category collation).

12  Guild Digest, 2015
13  ibid
14  It is The Pharmacy Guild of Australia’s position that the pharmacy channel should be a stand-alone Sales Group Category, in the same way that other unique retail operations are recognised by the Shopping Centre Council of Australia (SCCA) Guidelines, for example the Jewellery channel.
The Code is not intended to supersede any existing State & Territory legislation, however over time it is anticipated that this voluntary Code will be reflected in minimum lease standards nationally.

The main focus of the Code Administrative Committee of which the PGA is a member, is to introduce greater transparency as to how Landlords collate and report sales and occupancy cost data, so as to allow Lessee’s to better align their outcomes and benchmarks when negotiating leases.

It should be clearly noted, and in line with the Pharmacy Guild Guidelines for the Reporting of Sales to Landlords and the 2010 Shopping Centre Guidelines for Sales and Occupancy Cost Reporting that the exclusion of reporting any activity derived from the PBS or Pharmacy only sales is deliberate.

A legacy issue for Pharmacy Guild members is those Pharmacies who continue either deliberately or inadvertently to report PBS and Pharmacy only sales activity.

This single issue should be of concern to all members as it is a major cause of inflated rents for Pharmacy particularly in shopping centres.

Sales Productivity Measures

The SCCA Guidelines set out a number of Sales Productivity Measures, which are used by the property industry to produce industry benchmarks for occupancy costs. These benchmarks are used in property industry publications and reports to drive favourable promotion of the value of retail investments (both new and existing), mainly through the reporting of rental growth and returns for shareholders.

Treatment of GST

One sales productivity measure that has particular impact for community pharmacy is the treatment of GST. A standard property industry practice involves collating sales and occupancy costs that include GST in lessee sales reporting and then excluding GST in the occupancy charges of rent and outgoings etc. This treatment of GST results in occupancy cost measures which reflect a better than actual outcome in favour of the property industry.

HOW MUCH RENT CAN YOU AFFORD TO PAY?

Ultimately the business of pharmacy is no different to other businesses. Each owner needs to understand what the likely revenues are, the margin on those revenues, the costs to be incurred in carrying on business, and the profit that is generated. In addition, the owner will take into account the investment needed to operate the business and then assess whether the return on investment is sufficient.

RENT IS A FIXED COST

Occupancy costs are a fixed cost. Once the lease is signed, the overhead will not vary with turnover but instead will vary according to the terms of the lease. What is the percentage increase in rent, the share of overheads, marketing levies and any other outgoings to which you have agreed? These costs, over the term of the lease, can be relatively easily determined and set out. The challenge for an owner is to ascertain whether the revenues will be sufficient to generate returns that will cover these costs and the cost of doing business and leave a profit that will support the business’ balance sheet.

WHAT IS THE RENT WORTH – TO YOU?

Owners should not confuse the value of the real estate with the capacity of their business to pay the rent. Landlords, like pharmacy owners, are focused on return on investment. The real estate demands an acceptable return and, the landlords will say, the market will pay that return. Whether the business that is operated from that space will be able to afford the return is not an exercise that the landlord will undertake or guarantee. Whilst it is certainly in the landlord’s interest to have a tenant who can pay the rent, the landlord does not guarantee the performance of the space.

Owners should also distinguish between what turnover is needed to pay the rent and what turnover is likely to be generated. Once an owner can assess what the commitment will be to occupancy costs, this outlay will be part of your budget and you can ascertain what turnover is needed to provide a reasonable return on investment. The next step is the most important and difficult one – assessing what turnover is likely to be derived from the space.
BE REALISTIC

There are many factors which will feed into this assessment of rent. Location, competition, customer traffic, presence of prescribing medical practitioners, opening hours and type of pharmacy are just a few things to consider. Owners should consider various scenarios – pessimistic, moderate and optimistic – and see what working capital is needed in each instance to ensure their pharmacy is sustainable.

Owners should use this modelling to identify the daily sales targets needed in order to operate successfully. This will provide an instant target and a guide as to business performance.

Higher rents per square metre will obviously require higher sales targets just to break-even. This is further compounded if a large retail space is being considered.

With falling margins due to PBS reforms and strong competition in the health retail space, compounded by high fit-out costs to meet exacting landlord standards, owners need to be cognisant of the challenges that they face in seeking to achieve high multi-million dollar turnovers to cover costs.

BE WARY OF THE RATE OF INCREASE IN RENT

Rental increases can be significant over time. A 5% increase in rent means you need a 5% increase in turnover and constant margins in order to be in the same position. If your gross margin falls, as has happened with the impact of Price Disclosure, then you need a greater increase in turnover. If dispensary sales prices fall – and we should say ‘when’ and not ‘if’ – you will need a greater increase again to still be in the same position.

LOOK AT THE BIG PICTURE

Occupancy costs are but one part of your pharmacy business but they are significant and cannot be changed from week to week. Owners should ensure they are acutely aware of their business performance and know when a higher level of rent is simply not sustainable. It is important to be realistic in forecasting revenue and managing business costs to ensure that the resulting net profit is acceptable.

REPORTING TURNOVER FIGURES

Landlords typically use standard form leases which are not specific to pharmacy premises. These standard form leases will often include turnover rent provisions and provisions requiring the supply of turnover figures.

A long standing policy underpinning pharmacy regulation in Australia is that ownership of community pharmacies should remain in the hands of pharmacists. ‘Turnover rent’ is rent calculated in whole or part by reference to the turnover or profits of a business; the amount of rent varies depending on the sales results of the business. In effect, this type of rent gives the landlord a financial interest in the business.

Giving a landlord a financial interest in a pharmacy through a turnover rent provision runs counter to established policy. For this reason, pharmacy specific legislation in all Australian States prohibits or restricts turnover rent for pharmacy premises15:

FIGURE 1: State-Territory restrictions on the ‘turnover rent’ provisions

15 There are currently no restrictions on turnover rent in the Northern Territory and the Australian Capital Territory. Nevertheless, pharmacy owners in the Territories do have a legal right to negotiate rent arrangements with their landlord. Pharmacy owners, just like other retail shop owners, can seek to have a rent clause where rent is calculated on a basis other than turnover.
In leases for pharmacy premises, a turnover rent provision may well be excluded because of legal restrictions on turnover rent. However, the provisions requiring the supply of turnover figures often remain part of the lease. This situation presents an opportunity for landlords to refer to turnover figures when calculating rent.

Although turnover rent is prohibited or restricted in all Australian States, in some jurisdictions a landlord is not prevented from requiring a pharmacy owner to supply turnover figures (through reporting monthly sales results, for example). As a consequence, landlords may attempt to include a clause in a lease which requires pharmacy owners to provide turnover figures even when their lease does not include a turnover rent provision.

Including a turnover rent provision in a lease agreement for a pharmacy premise can result in significant consequences for both the landlord and the pharmacy owner, including financial penalties for the landlord. In some cases, a pharmacy owner’s ability to continue to carry out a pharmacy business at the premises may also be at risk. It is therefore important that members are aware of the prohibitions and restrictions on turnover rent when negotiating a new lease, renewing a lease, exercising an option under a lease or participating in a rent review process under an existing lease.

Members should think carefully before agreeing to supply turnover figures to their landlords. In most cases, agreeing to supply turnover figures will not be in the best interests of the pharmacy owner.

With this information in mind, if members do decide to provide turnover figures to their landlord, they should consider the most appropriate way to report turnover.

One option is to agree with your landlord that you will only report turnover based on sales in the general retail and scheduled non-prescription medicine categories (i.e. excluding sales of prescription medicines). In most (if not all) cases this condition will require an amendment to standard form leases to accommodate pharmacy specific provisions, including an appropriate definition of both ‘turnover’ or ‘gross sales’. Another option is to agree to provide turnover including prescription medicines, but with the exclusion of high cost drugs which artificially inflate turnover figures in relation to gross profit due to the very low margins available to pharmacies for these drugs.

If you have an existing lease that validly requires the provision of turnover figures, you must comply with the terms of that lease. However, you and your landlord could agree to a variation of the lease to accommodate changes in the way turnover is reported.

FIGURE 2: State-Territory restrictions on the provision of turnover information
EXPLANATORY NOTES

DEFINITION & TERMS - RENT & OUTGOINGS PER SQUARE METRE

RENT DEFINITION
Pharmacy rents are a major cost for all pharmacies. Careful negotiation and consideration of the benefits provided by a particular site must be taken into account when analysing the:

- Total occupancy costs (inc. outgoings)
- The terms of the lease (inc. security of tenure, exclusivity to the centre, escalation or indexation, options, and review periods/methods)
- The resultant share of profits derived by you and your landlord

In the broad terms, what is rent? Rent is the money or ‘consideration’ that the tenant pays a landlord for granting use or occupation of a property.

For a business person or shopping centre owner (or anyone), the rent is a monthly or an annual sum eg. $2,000 per month or $24,000 per annum. Many people say ‘My rent is $200 per square metre’ (’$/M2’). One should always calculate rent (gross rent with outgoings) back to an annual sum, as it is more relevant and can be related to the level of business (sales) that one can achieve.

OUTGOINGS DEFINITION
In addition to the rent, the tenant will often be responsible for reimbursing the landlord for outgoings payable under the lease, for example rates, use of services and costs of on-going cleaning and day to day repairs and maintenance. The landlord will generally pay for the repair or replacement of certain fixtures, fittings or equipment on the premises caused by fair wear and tear.

However, the above obligations are not standard to all leases and by no means apply to every situation. When negotiating a new lease it is imperative that the obligations of the landlord and the tenant are discussed and clearly reflected within the lease documents so that there is less likelihood of a dispute later on.

The landlord and tenant needs to be very clear on what outgoings are related to the leased premises, who is responsible for the payment of each outgoing and how will it be paid by either party. This must be documented in the lease and should be in plain English to remove any potential dispute. Similarly, the lease should contain provisions to explain if the outgoing costs will be increased in line rental reviews or another mechanism.

OPERATING EXPENSES
All retail businesses are subject to increasing operating expenses due to cost pressures across a range of business inputs. However the operating expenses of pharmacies are high and are more difficult to offset than for other retail businesses. Lessors need to have a clear understanding of pharmacies’ relatively limited ability to increase margins and recover increased costs, including the significant components associated with occupancy.

Salaries and stock are the main expense for pharmacies, reflecting the requirement to employ qualified pharmacists and to provide service and advice with regard to most products sold, as opposed to the customer self-selection or low service models of many other retailers. Governments contract with independent pharmacies as distribution agents for PBS approved medicines and health services. Strong commercial pressures exist to meet the required service standards which generate additional costs which are not typically faced by other retailers.

Rent comprises the second largest expense for pharmacy businesses and has increased substantially in both dollar and percentage terms over the last decade.

For a typical community pharmacy, the cost of goods sold (purchasing medicine and other stock to sell) comprises approximately two-thirds of their sales revenue. The remaining one third, the gross margin, is then required to pay for all operating expenses before a profit can be achieved for the business.

High stock holding costs have been amplified through the growing inclusion of high-cost medicines on the PBS, further increasing cost/profit ratios.
**EXPLANATORY NOTES**
(CONTINUED)

| **Confidence** | -95% and +95%
The estimated population mean for the variable taking account of the sample mean and size, and assuming a 95% statistical confidence in the estimate. |
| **Mean** | Average
The mean is one of several measures of central tendency that statisticians use to indicate the point on the scale of measures where the population is centred. The mean is the average of the scores in the population or sample. Numerically, it equals the sum of the scores divided by the number of scores. |
| **Median** | The median is the score located at the centre of a distribution. If the total number of values in the sample is even, then the median is the mean of the two middle numbers. The median is a useful number in cases where the distribution has very large extreme values which would otherwise skew the data or mean. |
| **n** | Sample number of observations. |
| **Rent & Outgoings** | Total Rent & Outgoings paid by the pharmacy per the lease document and rental invoice for the site. |
| **Turnover** | Annual sales for the pharmacy as reported for the relevant financial year. |
| **Shopping Centre Classifications** | Isolated | 1 to 4 shops  
Strip | 5 to 10 shops  
Neighbourhood | 10 to 20 shops  
Sub-Regional & Community | 20 to 50 shops  
Regional | 50 to 100 shops  
Major Regional | 100 plus shops |
## GLOSSARY

<table>
<thead>
<tr>
<th>Term</th>
<th>Description</th>
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<tbody>
<tr>
<td>CPI</td>
<td>Consumer price index.</td>
</tr>
<tr>
<td>Cost of goods sold</td>
<td>The amount paid to purchase goods for re-sale, including the cost of shipping and other costs directly related to the purchase of goods.</td>
</tr>
<tr>
<td>Early Determination of Market Rent</td>
<td>Restricted to QLD &amp; NSW for now. QLD refer to Retail Shop Leases Act 1994 Section 27A, NSW refer to Retail Leases Act 1994 section 32.</td>
</tr>
<tr>
<td>EBITA</td>
<td><em>Earnings before interest, tax, depreciation and amortization</em> EBITA is calculated by taking net profit before tax and adding back the expenses relating to interest, depreciation and amortization. It provides an indication of profitability eliminating the effects of financing and accounting decisions.</td>
</tr>
<tr>
<td>Expense</td>
<td>All expense items, expressed as a percentage of total revenue.</td>
</tr>
<tr>
<td>Front of shop (FOS)</td>
<td><em>Front of shop (FOS)</em> or retail sales are total sales less dispensary sales</td>
</tr>
<tr>
<td>Gross lettable area retail (GLAR)</td>
<td>A measure of the amount of retail space within a shopping centre, commercial building or strip centre available for lease. GLAR is the total floor space available for lease measured from the outside walls. GLAR is used for calculating tenancy areas in shopping centres, strip centres, and commercial buildings.</td>
</tr>
<tr>
<td>Gross margin</td>
<td><em>Gross margin</em> is the income from which operating expenses are paid, and remaining profit derived. Gross margin is calculated by deducting cost of goods sold from sales.</td>
</tr>
<tr>
<td>Gross Margin Plus Other Income</td>
<td>The arithmetic total of the gross margin and other income. Represents the total gross margin from trading.</td>
</tr>
<tr>
<td>GST</td>
<td>Goods and Services Tax</td>
</tr>
<tr>
<td>Large shopping centre</td>
<td>A large shopping centre typically incorporates at least one department store, one or more discount stores, one or more supermarkets and approximately 100 specialty shops.</td>
</tr>
<tr>
<td>Lease</td>
<td>The lease is the document detailing all the terms agreed between the Lessor and the Lessee.</td>
</tr>
<tr>
<td>Lessee</td>
<td>The person or organisation who rents land or property. Also known as the tenant.</td>
</tr>
<tr>
<td>Lessor</td>
<td>The person or organisation who grants a lease. Also known as the landlord or property owner.</td>
</tr>
<tr>
<td>Major tenancy</td>
<td>Tenancies generally greater than 1,000 square metres (GLAR) that occupy the largest space of any single tenancy in the centre and are considered major attractions to the centre by customers.</td>
</tr>
<tr>
<td>Medical centre</td>
<td>A medical centre is an establishment housing a group of doctors offering healthcare services from a single premises.</td>
</tr>
<tr>
<td>Mini Major</td>
<td>All tenants greater than 400sqm not defined as Major, Other Retail or Non Retail. Some pharmacies in shopping centres have a GLAR over 400m2 and hence need to be treated as a Mini Major and not a Speciality Retailer for the purposes of rental and shop fit requirements.</td>
</tr>
<tr>
<td>Moving Annual Turnover (MAT)</td>
<td>Sales for a twelve-month period calculated on a monthly basis. MAT = preceding 12 months sales including the most current available month minus the corresponding month from the previous year.</td>
</tr>
<tr>
<td>Occupancy Cost Ratio</td>
<td>Occupancy costs for the premises divided by the <em>Moving Annual Turnover</em> and expressed as a percentage. Calculated by dividing the tenant’s total occupancy costs into their gross turnover.</td>
</tr>
</tbody>
</table>
### GLOSSARY (CONTINUED)

<table>
<thead>
<tr>
<th><strong>Other Income</strong></th>
<th>Income from items which do not involve cost of goods sold, including that derived from Community Pharmacy Agreement programs or professional services. Dividend and rent income, and other such income not connected with the pharmacy's operation are also included here.</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Operating expenses</strong></td>
<td>Expenditure that a business incurs as a result of performing its normal business operations.</td>
</tr>
<tr>
<td><strong>Outgoings</strong></td>
<td>Outgoings are expenses relating to the retail space including, but are not necessarily limited to, rates, strata levies, insurances, land tax, repairs and maintenance, and management fees. Your retail lease may have a special definition and rules about outgoings.</td>
</tr>
<tr>
<td><strong>PBS</strong></td>
<td>Pharmaceutical Benefits Scheme</td>
</tr>
<tr>
<td><strong>Rent</strong></td>
<td>Rent is a periodic payment by a lessee to a lessor for the use of land or property. Rent is shown in this report exclusive of occupancy cost and GST.</td>
</tr>
<tr>
<td><strong>Revenue</strong></td>
<td>Revenue is income that a business receives from its normal business activities. Also known as turnover.</td>
</tr>
<tr>
<td><strong>Salaries and Wages</strong></td>
<td>Includes wages paid to all staff and locums excluding proprietors' earnings (since the latter are represented by proprietors' notional salary). Expressed as a percentage of total revenue.</td>
</tr>
<tr>
<td><strong>Sales</strong></td>
<td>Sales relate to the sale of all products (both prescription and retail) for which goods were purchased at wholesale for the purpose of re-sale at a profit.</td>
</tr>
<tr>
<td><strong>Services income</strong></td>
<td>Includes government payments such as rural allowances, trade rebates, discounts, commissions, agency fees, dividends and disposal of assets are excluded.</td>
</tr>
<tr>
<td><strong>Scheduled medicines</strong></td>
<td>Pharmaceutical products that are only available from a pharmacy because of the potency and safety profile of the medicine.</td>
</tr>
<tr>
<td><strong>Shopping strip</strong></td>
<td>A shopping strip is where shops are arranged in a row with a footpath in front of the shop. There are usually multiple landlords.</td>
</tr>
<tr>
<td><strong>Small shopping centre</strong></td>
<td>A small shopping centre typically incorporates at least one full time discount department store, a major supermarket and at least 40 specialty shops.</td>
</tr>
<tr>
<td><strong>Total centre area retail</strong></td>
<td>The aggregation of all lettable areas in a shopping centre retail, commercial and miscellaneous.</td>
</tr>
<tr>
<td><strong>Total centre lettable area</strong></td>
<td>The aggregation of all lettable areas in a shopping centre retail, commercial and miscellaneous.</td>
</tr>
<tr>
<td><strong>Total income</strong></td>
<td>Arrived at by subtracting total expenses and cost of goods sold from total revenue, it refers to the trading profit of the pharmacy which may involve several partners. Percentage shown is of total revenue.</td>
</tr>
<tr>
<td><strong>Total Revenue</strong></td>
<td>The arithmetic total of sales and other income; all expenses are expressed as a percentage of total revenue not sales) since a portion of all expenses is also incurred in earning other income.</td>
</tr>
<tr>
<td><strong>Turnover</strong></td>
<td>Turnover is income that a business receives from its normal business activities. Also referred to as revenue.</td>
</tr>
<tr>
<td><strong>Turnover/Sales Per Square Metre</strong></td>
<td>Sales divided by the total number of square metres of rentable area. May apply to individual stores, groups of stores or the total centre.</td>
</tr>
</tbody>
</table>
# SHOPPING CENTRE CLASSIFICATIONS

<table>
<thead>
<tr>
<th>CLASSIFICATION</th>
<th>DEFINITION</th>
<th>KEY FEATURES</th>
</tr>
</thead>
</table>
| City centre             | Retail premises within an arcade or mall development owned by one company, firm or person and promoted as an entity within a major central business district. The total gross lettable area retail exceeds 1,000 square metres.                                                                                                                                   | • Dominated by specialty shops  
• Likely to have frontage on a mall or major CBD road  
• Generally do not include supermarkets  
• Often co-exists with large department stores.                                                                                                                                                                                                                                                                                       |
| Super regional centre   | A major shopping centre typically incorporating two full line department stores, one or more full line discount department stores, two supermarkets and approximately 250 specialty shops. The total gross lettable area retail exceeds 85,000 square metres.                                                                                                                                       | • One-stop shopping for all needs  
• Comprehensive coverage of the full range of retail needs (including specialised retail), containing a combination of full line department stores, full line discount department stores, supermarkets, services, chain and other specialty retailers  
• Typically includes a number of entertainment and leisure attractions such as cinemas, arcade games and soft play centres  
• Provides a broad range of shopper facilities (car parking, food court) and amenities (rest rooms, seating).                                                                                                                                                                                                 |
| Major regional centre   | A major shopping centre typically incorporating at least one full line department store, one or more full line discount department stores, one or more supermarkets and approximately 150 specialty shops. The total gross lettable area retail ranges between 50,000 and 85,000 square metres.                                                                                                                               | • One-stop shopping for all needs  
• Extensive coverage of the full range of retail needs (including specialised retail), containing a combination of full line department stores, full line discount department stores, supermarkets, services, chain and other specialty retailers  
• Typically includes a number of entertainment and leisure attractions such as cinemas, arcade games and soft play centres  
• Provides a broad range of shopper facilities (car parking, food court) and amenities (rest rooms, seating).                                                                                                                                                                                                 |
| Regional centre         | A shopping centre typically incorporates one full line department store, a full line discount department store, one or more supermarkets and approximately 100 specialty shops. Total gross lettable area retail ranges between 30,000 and 50,000 square metres. In some instances, all other characteristics being equal, a centre with two full line discount department stores, without a department store, serves as a regional centre. | • Extensive coverage of a broad range of retail needs (including specialised retail), however, not as exhaustive as major regional centres  
• Contains a combination of full line department stores, full line discount department stores, supermarkets, banks, chain and other specialty retailers  
• Provides a broad range of shopper facilities and amenities.                                                                                                                                                                                                                                                                              |
### SHOPPING CENTRE CLASSIFICATIONS

(Continued)

<table>
<thead>
<tr>
<th>CLASSIFICATION</th>
<th>DEFINITION</th>
<th>KEY FEATURES</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sub-regional centre</td>
<td>A medium sized shopping centre typically incorporating at least one full line discount department store, a major supermarket and approximately 40 specialty shops. Total gross lettable area retail ranges between 10,000 and 30,000 square metres.</td>
<td>• Provides a broad range of sub-regional retail needs&lt;br&gt;• Typically dominated by a full line discount department store or major supermarket.</td>
</tr>
<tr>
<td>Neighbourhood centre</td>
<td>A local shopping centre comprising a supermarket and approximately 35 specialty shops. The total gross lettable area retail is less than 10,000 square metres.</td>
<td>• Typically located in residential areas&lt;br&gt;• Services an immediate residential neighbourhood&lt;br&gt;• Usually has extended trading hours&lt;br&gt;• Caters for basic day-to-day retail needs.</td>
</tr>
<tr>
<td>Bulky goods centre</td>
<td>A medium to large sized shopping centre dominated by bulky goods retailers (furniture, white goods and other home wares), occupying large areas to display merchandise. Typically contain a small number of specialty shops. The total gross lettable area retail is generally greater than 5,000 square metres in size.</td>
<td>• Generally located adjacent to large regional centres or in non-traditional retail locations (i.e. greenfield sites and industrial areas)&lt;br&gt;• Purpose designed, built and operated, generally with a layout of outlets around a central, landscaped area and an overall design and colour theme to promote the appearance of an integrated development.</td>
</tr>
<tr>
<td>Specialty store</td>
<td>A non-major retail shop in a centre that specialises in a narrow range of merchandise with an emphasis on product knowledge and customer service. Shops usually range up to 400 square metres.</td>
<td></td>
</tr>
<tr>
<td>Themed centre</td>
<td>A specialty shopping centre, located primarily in resort areas to cater for specialist tourist needs, which does not normally include a supermarket.</td>
<td>• A resort or tourist style development.&lt;br&gt;• The size of the centre is not a determining factor.&lt;br&gt;• Comprise mainly specialty shops with food courts.</td>
</tr>
<tr>
<td>Market</td>
<td>A covered centre of at least 5,000 square metres dominated by food retailing with at least 50 stalls or outlets. It operates on a permanent or irregular basis.</td>
<td>• Includes areas with refrigeration facilities and air conditioning as well as areas without these facilities.</td>
</tr>
<tr>
<td>Outlet centre</td>
<td>A medium to large sized shopping centre which does not normally include a department store, discount department store, or supermarket.</td>
<td>• Comprise specialty shops often selling stock at discounted prices including samples, seconds and discontinued lines.</td>
</tr>
<tr>
<td>Enclosed mall</td>
<td>A shopping centre that has an enclosed retail area, is air-conditioned and is entered from a surrounding car park that forms part of the property.</td>
<td></td>
</tr>
</tbody>
</table>
2019 PHARMACY RENTAL REPORT

PART TWO / LEASING BENCHMARKS
RENTAL / LEASING BENCHMARKS

What is a benchmark? A benchmark is comparing one’s business processes and performance metrics to industry best practices from other companies. It is a reference point by which something can be measured and compared against to assist in the decision-making process.

Benchmarking is a useful tool to ensure that credible goals, objectives and directions are set and in deciding whether or not to lease certain premises.

Benchmarking can also be used to ascertain the occupancy costs (rent and outgoings) of a similar type of business, in order to achieve an acceptable profit.

Community pharmacy premises vary in size and in their allocation of floor space.

Rates per square metre vary dramatically by State/Territory and location. Prices vary considerably by the type of location, with pharmacies located in large medical centres and large shopping centres being the most expensive per square metre. Similarly, pharmacies in metropolitan areas pay considerably more per square metre than pharmacies located in non-metropolitan areas.

Consider the location and state of your pharmacy, and whether it is in a metropolitan or non-metropolitan location.

GENERAL BENCHMARKS

PHARMACY MARKET

Pharmacy rents and occupancy costs represent a significant and increasing cost of pharmacy operations. Indeed, after cost of goods sold, it is usually the next highest expense after staffing costs. For some pharmacies the landlord earns more from the pharmacy than its owners do.

Pharmacy often pays a premium rent in most locations despite being a low risk tenant with a keen interest in developing the location and site. In the light of recent PBS Reforms, Price Disclosure and competitive retail environment, pharmacists will increasingly need quantifiable data to confirm suitable ranges for tenancy negotiations.

AUSTRALIAN TAX OFFICE BENCHMARK

The Australian Tax Office (ATO) defines ‘Pharmacy’ as businesses that sell prescription medication, medical accessories and other health care products. They may also sell beauty and personal care products, confectionary and gift items.

The ATO has developed several performance benchmarks from the information reported on tax returns and activity statements for the 2015–16 financial year, and these are updated each year. These benchmarks do not apply to businesses that only provide labour and management services to pharmacies.

Cost of sales to turnover is the key benchmark range for this industry – it is likely to be the most accurate when predicting business turnover. If you don’t report cost of sales, or only report a small amount, use total expenses to turnover as your key benchmark range instead.

The ATO benchmark performance indicator for Rent/ Turnover for the financial year 2015-16 is a range of 3% to 5%. Similarly, the ATO benchmark range for Labour/ Turnover has a range of 9% to 14%.

BENCHMARKS

In 2007, a Medici Capital report on Australian community pharmacy average rent and outgoings per square metre (per annum) indicated that the average rent was $544.69 (95% confidence interval ranges from $491 to $599) with the average rent as a percentage of turnover was 4.19% (95% confidence interval ranges from 3.85% to 4.52%).

In 2018, a similar report on Australian average rent and outgoings per square metre (per annum) was $667 (95% confidence interval ranges from $592 to $742) with the average rent as a percentage of turnover being 4.98% (95% confidence interval ranges from 4.41% to 5.55%).

Therefore in 2018, the average rent and outgoings per square (per annum) for community pharmacy has increased by approximately $123.00 with the average rent as a percentage of turnover has increased by 0.79 basis points.
**PHARMACY RENT DATA**

**PHARMACY RENT AND OUTGOINGS PER SQUARE METRE**

**TABLE 1: Rent & Outgoings per square metre per annum – FY2018**

<table>
<thead>
<tr>
<th>LOCATION</th>
<th>LOW RANGE</th>
<th>AVERAGE</th>
<th>HIGH RANGE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Metro</td>
<td>$736</td>
<td>$831</td>
<td>$925</td>
</tr>
<tr>
<td>Rural</td>
<td>$264</td>
<td>$337</td>
<td>$409</td>
</tr>
<tr>
<td>All Locations</td>
<td>$592</td>
<td>$667</td>
<td>$742</td>
</tr>
</tbody>
</table>

**TABLE 2: Rent & Outgoings per square metre per annum – FY2017**

<table>
<thead>
<tr>
<th>LOCATION</th>
<th>LOW RANGE</th>
<th>AVERAGE</th>
<th>HIGH RANGE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Metro</td>
<td>$813</td>
<td>$891</td>
<td>$969</td>
</tr>
<tr>
<td>Rural</td>
<td>$328</td>
<td>$391</td>
<td>$454</td>
</tr>
<tr>
<td>All Locations</td>
<td>$671</td>
<td>$732</td>
<td>$792</td>
</tr>
</tbody>
</table>

Compared to FY2017, the average rent and outgoings per square metre experienced a 9.70% decrease across all locations. This decrease was higher for pharmacies located in rural areas (14.8%) than for those in metropolitan areas (6.9%). Distribution of rent and outgoings per square metre is noted to be within a small range for the majority of pharmacies, with small numbers of pharmacies paying very high rents. The presence of a small number of pharmacies with very high rent and outgoings per square metre subsequently tend to distort estimates of the average rent paid by pharmacies.

**FIGURE 3: Distribution of Rent & Outgoings per square metre - FY2018**

Source: Medici Capital data

*Caution is advised when interpreting the annual change between rates for the benchmark figures in the following tables, due to significant change in sample size for the two periods.*
Rent and outgoings as proportion of turnover remained fairly constant between 2017 and 2018, with a slight increase for the average pharmacy of 0.18%. This increase was driven by rural pharmacies, with the proportion of turnover consumed by rent and outgoings increasing at the low range whilst decreasing in the high range for metropolitan pharmacies.

### FIGURE 4: Distribution of Rent & Outgoings % - FY2018

Source: Medici Capital data
**PHARMACY RENTAL DISTRIBUTION**

**TABLE 5: Quartile Analysis Rent & Outgoings – FY2018**

<table>
<thead>
<tr>
<th>QUARTILE ANALYSIS</th>
<th>25%</th>
<th>50%</th>
<th>75%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rent &amp; Outgoings</td>
<td>$277</td>
<td>$537</td>
<td>$847</td>
</tr>
<tr>
<td>per square metre</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(PSM) per annum</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Rent &amp; Outgoings</td>
<td>2.55%</td>
<td>3.73%</td>
<td>6.03%</td>
</tr>
<tr>
<td>% Turnover</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**TABLE 6: Quartile Analysis Rent & Outgoings – FY2017**

<table>
<thead>
<tr>
<th>QUARTILE ANALYSIS</th>
<th>25%</th>
<th>50%</th>
<th>75%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rent &amp; Outgoings</td>
<td>$334</td>
<td>$585</td>
<td>$958</td>
</tr>
<tr>
<td>per square metre</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>(PSM) per annum</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Rent &amp; Outgoings</td>
<td>2.58%</td>
<td>4.18%</td>
<td>6.87%</td>
</tr>
<tr>
<td>% Turnover</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Rental distribution by quartile showed a decreasing range for rent and outgoings per square metre (psm) in dollar terms in 2018 when compared to 2017, indicating a smaller range of rents paid by pharmacies across all locations. The range for rent and outgoings as a percentage of turnover remained reasonably constant, but experienced a shift towards slightly higher values overall.

**PHARMACY RENT & OUTGOINGS PER SQUARE METRE BY STATE & LOCATION**

**TABLE 7: Rent & Outgoings per square metre per annum – FY2018**

<table>
<thead>
<tr>
<th>STATE</th>
<th>LOCATION</th>
<th>LOW RANGE</th>
<th>AVERAGE</th>
<th>HIGH RANGE</th>
</tr>
</thead>
<tbody>
<tr>
<td>VIC</td>
<td>Metropolitan</td>
<td>$690</td>
<td>$816</td>
<td>$942</td>
</tr>
<tr>
<td>VIC</td>
<td>Rural</td>
<td>$217</td>
<td>$287</td>
<td>$358</td>
</tr>
<tr>
<td>QLD</td>
<td>Metropolitan</td>
<td>$614</td>
<td>$764</td>
<td>$914</td>
</tr>
<tr>
<td>QLD</td>
<td>Rural</td>
<td>$5</td>
<td>$437</td>
<td>$870</td>
</tr>
<tr>
<td>NSW</td>
<td>Metropolitan</td>
<td>$823</td>
<td>$1,155</td>
<td>$1,486</td>
</tr>
<tr>
<td>NSW</td>
<td>Rural</td>
<td>$214</td>
<td>$433</td>
<td>$652</td>
</tr>
<tr>
<td>Australia Wide</td>
<td><strong>$592</strong></td>
<td>$667</td>
<td>$742</td>
<td></td>
</tr>
</tbody>
</table>

**TABLE 8: Rent & Outgoings per square metre per annum – FY2017**

<table>
<thead>
<tr>
<th>STATE</th>
<th>LOCATION</th>
<th>LOW RANGE</th>
<th>AVERAGE</th>
<th>HIGH RANGE</th>
</tr>
</thead>
<tbody>
<tr>
<td>VIC</td>
<td>Metropolitan</td>
<td>$726</td>
<td>$805</td>
<td>$884</td>
</tr>
<tr>
<td>VIC</td>
<td>Rural</td>
<td>$238</td>
<td>$284</td>
<td>$330</td>
</tr>
<tr>
<td>QLD</td>
<td>Metropolitan</td>
<td>$662</td>
<td>$950</td>
<td>$1,238</td>
</tr>
<tr>
<td>QLD</td>
<td>Rural</td>
<td>$403</td>
<td>$613</td>
<td>$823</td>
</tr>
<tr>
<td>NSW</td>
<td>Metropolitan</td>
<td>$1,007</td>
<td>$1,179</td>
<td>$1,351</td>
</tr>
<tr>
<td>NSW</td>
<td>Rural</td>
<td>$301</td>
<td>$429</td>
<td>$557</td>
</tr>
<tr>
<td>Australia Wide</td>
<td><strong>$671</strong></td>
<td>$732</td>
<td>$792</td>
<td></td>
</tr>
</tbody>
</table>

**19 East Coast only.**
### PHARMACY RENT DATA
(CONTINUED)

### PHARMACY RENT & OUTGOINGS PER SQUARE METRE BY SHOPPING CENTRE TYPE

**TABLE 9:** Rent & Outgoings psm by Shopping Centre Type – FY2018

<table>
<thead>
<tr>
<th>SHOPPING CENTRE TYPE</th>
<th>LOW RANGE</th>
<th>AVERAGE</th>
<th>HIGH RANGE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Isolated</td>
<td>$64</td>
<td>$318</td>
<td>$571</td>
</tr>
<tr>
<td>Strip</td>
<td>$232</td>
<td>$430</td>
<td>$629</td>
</tr>
<tr>
<td>Neighbourhood</td>
<td>$418</td>
<td>$511</td>
<td>$605</td>
</tr>
<tr>
<td>Sub-Regional &amp; Community</td>
<td>$532</td>
<td>$653</td>
<td>$774</td>
</tr>
<tr>
<td>Regional</td>
<td>$444</td>
<td>$636</td>
<td>$827</td>
</tr>
<tr>
<td>Major Regional</td>
<td>$998</td>
<td>$1,356</td>
<td>$1,715</td>
</tr>
<tr>
<td>Medical Centre</td>
<td>$630</td>
<td>$1,055</td>
<td>$1,481</td>
</tr>
<tr>
<td>All Locations</td>
<td>$592</td>
<td>$667</td>
<td>$742</td>
</tr>
</tbody>
</table>

**TABLE 10:** Rent & Outgoings psm by Shopping Centre Type – FY2017

<table>
<thead>
<tr>
<th>SHOPPING CENTRE TYPE</th>
<th>LOW RANGE</th>
<th>AVERAGE</th>
<th>HIGH RANGE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Isolated</td>
<td>$144</td>
<td>$359</td>
<td>$574</td>
</tr>
<tr>
<td>Strip</td>
<td>$324</td>
<td>$451</td>
<td>$578</td>
</tr>
<tr>
<td>Neighbourhood</td>
<td>$462</td>
<td>$524</td>
<td>$585</td>
</tr>
<tr>
<td>Sub-Regional &amp; Community</td>
<td>$566</td>
<td>$639</td>
<td>$712</td>
</tr>
<tr>
<td>Regional</td>
<td>$660</td>
<td>$820</td>
<td>$981</td>
</tr>
<tr>
<td>Major Regional</td>
<td>$1,193</td>
<td>$1,512</td>
<td>$1,830</td>
</tr>
<tr>
<td>Medical Centre</td>
<td>$779</td>
<td>$1,045</td>
<td>$1,311</td>
</tr>
<tr>
<td>All Locations</td>
<td>$671</td>
<td>$732</td>
<td>$792</td>
</tr>
</tbody>
</table>

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*Data is based upon Eastern Australia*
RENTAL CONTRACTUAL INCREASES VS CONSUMER PRICE INDEX (CPI)

From a landlord’s perspective, rent reviews are an essential component of a commercial lease. Reviewing the rent at specified intervals ensures that the rent keeps pace with current market rates.

The Consumer Price Index (CPI) produced by the Australian Bureau of Statistics (ABS) measures quarterly changes in the price of a ‘basket’ of goods and services which account for a high proportion of expenditure by the CPI population group (i.e. metropolitan households). This ‘fixed basket’ covers a wide range of goods and services.

The CPI affects almost all Australians because of the many ways it is used. It is primarily used as a macro-economic indicator by the government and economists to monitor and evaluate levels of inflation in the Australian economy, and for adjusting dollar values of types of fixed payments, such as pensions and contracts.

Rental contractual increases are either a fixed amount or the amount negotiated into the leasing contract to be reviewed each year. Figure 5 below shows the difference in trends between retail rent and CPI, with growth in retail rent outstripping CPI growth by an increasing amount year on year. It should be noted that since 2014, there has been a minimal increase to the CPI rate when compared to the retail rent trend.

FIGURE 5: Comparison of Consumer Price Index and annual increases in retail rent, FY2007–FY2018

Source: Guild Digest 2000 – Guild Digest 2014, ABS 8501.0 June 2014

Note: In 2009 changes to the sampling procedure introduced re-standardised weightings which caused a data anomaly. This result has been standardised in the above figure.
The median rent per square metre paid by pharmacies has been increasing in recent years. Data shows that the median rent per square metre has increased by around $150 between 2013 and 2018. Median rents have, however, fallen in the recent year by around $50.00. Figure 6 demonstrates median rent and outgoings per square metre over the previous 7 years. The trend shows overall positive growth during the period.

**FIGURE 6:** Rent and Outgoings psm, by Financial Year

Source: Medici Capital data
EXPLANATORY NOTES

DEFINITION & TERMS - RENT & OUTGOINGS PER SQUARE METRE

RENT DEFINITION

Pharmacy rents are a major cost for all pharmacies. Careful negotiation and consideration of the benefits provided by a particular site must be taken into account when analysing the:

- Total occupancy costs (inc. outgoings)
- The terms of the lease (inc. security of tenure, exclusivity to the centre, escalation or indexation, options, and review periods/methods)
- The resultant share of profits derived by you and your landlord

In the broad terms, what is rent? Rent is the money or ‘consideration’ that the tenant pays a landlord for granting use or occupation of a property.

For a business person or shopping centre owner (or anyone), the rent is a monthly or an annual sum eg. $2,000 per month or $24,000 per annum. Many people say ‘My rent is $200 per square metre’ (‘$/M2’). One should always calculate rent (gross rent with outgoings) back to an annual sum, as it is more relevant and can be related to the level of business (sales) that one can achieve.

OUTGOINGS DEFINITION

In addition to the rent, the tenant will often be responsible for reimbursing the landlord for outgoings payable under the lease, for example rates, use of services and costs of on-going cleaning and day to day repairs and maintenance. The landlord will generally pay for the repair or replacement of certain fixtures, fittings or equipment on the premises caused by fair wear and tear.

However, the above obligations are not standard to all leases and by no means apply to every situation. When negotiating a new lease it is imperative that the obligations of the landlord and the tenant are discussed and clearly reflected within the lease documents so that there is less likelihood of a dispute later on.

The landlord and tenant needs to be very clear on what outgoings are related to the leased premises, who is responsible for the payment of each outgoing and how will it be paid by either party. This must be documented in the lease and should be in plain English to remove any potential dispute. Similarly, the lease should contain provisions to explain if the outgoing costs will be increased in line rental reviews or another mechanism.

OPERATING EXPENSES

All retail businesses are subject to increasing operating expenses due to cost pressures across a range of business inputs. However the operating expenses of pharmacies are high and are more difficult to offset than for other retail businesses. Lessors need to have a clear understanding of pharmacies’ relatively limited ability to increase margins and recover increased costs, including the significant components associated with occupancy.

Salaries and stock are the main expense for pharmacies, reflecting the requirement to employ qualified pharmacists and to provide service and advice with regard to most products sold, as opposed to the customer self-selection or low service models of many other retailers. Governments contract with independent pharmacies as distribution agents for PBS approved medicines and health services. Strong commercial pressures exist to meet the required service standards which generate additional costs which are not typically faced by other retailers.

Rent comprises the second largest expense for pharmacy businesses and has increased substantially in both dollar and percentage terms over the last decade.

For a typical community pharmacy, the cost of goods sold (purchasing medicine and other stock to sell) comprises approximately two-thirds of their sales revenue. The remaining one third, the gross margin, is then required to pay for all operating expenses before a profit can be achieved for the business.

High stock holding costs have been amplified through the growing inclusion of high-cost medicines on the PBS, further increasing cost/profit ratios.
EXPLANATORY NOTES
(CONTINUED)

<table>
<thead>
<tr>
<th>Confidence</th>
<th>-95% and +95%</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>The estimated population mean for the variable taking account of the sample mean and size, and assuming a 95% statistical confidence in the estimate.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Mean</th>
<th>Average</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>The mean is one of several measures of central tendency that statisticians use to indicate the point on the scale of measures where the population is centred. The mean is the average of the scores in the population or sample. Numerically, it equals the sum of the scores divided by the number of scores.</td>
</tr>
</tbody>
</table>

| Median          | The median is the score located at the centre of a distribution. If the total number of values in the sample is even, then the median is the mean of the two middle numbers. The median is a useful number in cases where the distribution has very large extreme values which would otherwise skew the data or mean. |

| n               | Sample number of observations. |

| Rent & Outgoings| Total Rent & Outgoings paid by the pharmacy per the lease document and rental invoice for the site. |

| Turnover        | Annual sales for the pharmacy as reported for the relevant financial year. |

<table>
<thead>
<tr>
<th>Shopping Centre Classifications</th>
<th>Isolated</th>
<th>1 to 4 shops</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Strip</td>
<td>5 to 10 shops</td>
</tr>
<tr>
<td></td>
<td>Neighbourhood</td>
<td>10 to 20 shops</td>
</tr>
<tr>
<td></td>
<td>Sub-Regional &amp; Community</td>
<td>20 to 50 shops</td>
</tr>
<tr>
<td></td>
<td>Regional</td>
<td>50 to 100 shops</td>
</tr>
<tr>
<td></td>
<td>Major Regional</td>
<td>100 plus shops</td>
</tr>
<tr>
<td><strong>GLOSSARY</strong></td>
<td></td>
<td></td>
</tr>
<tr>
<td>----------------</td>
<td>-----------------</td>
<td></td>
</tr>
<tr>
<td><strong>CPI</strong></td>
<td>Consumer price index.</td>
<td></td>
</tr>
<tr>
<td><strong>Cost of goods sold</strong></td>
<td>The amount paid to purchase goods for re-sale, including the cost of shipping and other costs directly related to the purchase of goods.</td>
<td></td>
</tr>
<tr>
<td><strong>Early Determination of Market Rent</strong></td>
<td>Restricted to QLD &amp; NSW for now. QLD refer to Retail Shop Leases Act 1994 Section 27A, NSW refer to Retail Leases Act 1994 section 32.</td>
<td></td>
</tr>
<tr>
<td><strong>EBITA</strong></td>
<td><em>Earnings before interest, tax, depreciation and amortization</em> EBITA is calculated by taking net profit before tax and adding back the expenses relating to interest, depreciation and amortization. It provides an indication of profitability eliminating the effects of financing and accounting decisions.</td>
<td></td>
</tr>
<tr>
<td><strong>Expense</strong></td>
<td>All expense items, expressed as a percentage of total revenue.</td>
<td></td>
</tr>
<tr>
<td><strong>Front of shop (FOS)</strong></td>
<td><em>Front of shop</em> (FOS) or retail sales are total sales less dispensary sales</td>
<td></td>
</tr>
<tr>
<td><strong>Gross lettable area retail (GLAR)</strong></td>
<td>A measure of the amount of retail space within a shopping centre, commercial building or strip centre available for lease. GLAR is the total floor space available for lease measured from the outside walls. GLAR is used for calculating tenancy areas in shopping centres, strip centres, and commercial buildings.</td>
<td></td>
</tr>
<tr>
<td><strong>Gross margin</strong></td>
<td><em>Gross margin</em> is the income from which operating expenses are paid, and remaining profit derived. Gross margin is calculated by deducting cost of goods sold from sales.</td>
<td></td>
</tr>
<tr>
<td><strong>Gross Margin Plus Other Income</strong></td>
<td>The arithmetic total of the gross margin and other income. Represents the total gross margin from trading.</td>
<td></td>
</tr>
<tr>
<td><strong>GST</strong></td>
<td>Goods and Services Tax</td>
<td></td>
</tr>
<tr>
<td><strong>Large shopping centre</strong></td>
<td>A large shopping centre typically incorporates at least one department store, one or more discount stores, one or more supermarkets and approximately 100 specialty shops.</td>
<td></td>
</tr>
<tr>
<td><strong>Lease</strong></td>
<td>The lease is the document detailing all the terms agreed between the Lessor and the Lessee.</td>
<td></td>
</tr>
<tr>
<td><strong>Lessee</strong></td>
<td>The person or organisation who rents land or property. Also known as the tenant.</td>
<td></td>
</tr>
<tr>
<td><strong>Lessor</strong></td>
<td>The person or organisation who grants a lease. Also known as the landlord or property owner.</td>
<td></td>
</tr>
<tr>
<td><strong>Major tenancy</strong></td>
<td>Tenancies generally greater than 1,000 square metres (GLAR) that occupy the largest space of any single tenancy in the centre and are considered major attractions to the centre by customers.</td>
<td></td>
</tr>
<tr>
<td><strong>Medical centre</strong></td>
<td>A medical centre is an establishment housing a group of doctors offering healthcare services from a single premises.</td>
<td></td>
</tr>
<tr>
<td><strong>Mini Major</strong></td>
<td>All tenants greater than 400sqm not defined as Major, Other Retail or Non Retail. Some pharmacies in shopping centres have a GLAR over 400m2 and hence need to be treated as a Mini Major and not a Speciality Retailer for the purposes of rental and shop fit requirements.</td>
<td></td>
</tr>
<tr>
<td><strong>Moving Annual Turnover (MAT)</strong></td>
<td>Sales for a twelve-month period calculated on a monthly basis. MAT = preceding 12 months sales including the most current available month minus the corresponding month from the previous year.</td>
<td></td>
</tr>
<tr>
<td><strong>Occupancy Cost Ratio</strong></td>
<td>Occupancy costs for the premises divided by the <em>Moving Annual Turnover</em> and expressed as a percentage. Calculated by dividing the tenant’s total occupancy costs into their gross turnover.</td>
<td></td>
</tr>
</tbody>
</table>
### Glossary (Continued)

<table>
<thead>
<tr>
<th>Term</th>
<th>Definition</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Other Income</strong></td>
<td>Income from items which do not involve cost of goods sold, including that derived from Community Pharmacy Agreement programs or professional services. Dividend and rent income, and other such income not connected with the pharmacy’s operation are also included here.</td>
</tr>
<tr>
<td><strong>Operating expenses</strong></td>
<td>Expenditure that a business incurs as a result of performing its normal business operations.</td>
</tr>
<tr>
<td><strong>Outgoings</strong></td>
<td>Outgoings are expenses relating to the retail space including, but are not necessarily limited to, rates, strata levies, insurances, land tax, repairs and maintenance, and management fees. Your retail lease may have a special definition and rules about outgoings.</td>
</tr>
<tr>
<td><strong>PBS</strong></td>
<td>Pharmaceutical Benefits Scheme</td>
</tr>
<tr>
<td><strong>Rent</strong></td>
<td>Rent is a periodic payment by a lessee to a lessor for the use of land or property. Rent is shown in this report exclusive of occupancy cost and GST.</td>
</tr>
<tr>
<td><strong>Revenue</strong></td>
<td>Revenue is income that a business receives from its normal business activities. Also known as turnover.</td>
</tr>
<tr>
<td><strong>Salaries and Wages</strong></td>
<td>Includes wages paid to all staff and locums excluding proprietors’ earnings (since the latter are represented by proprietors’ notional salary). Expressed as a percentage of total revenue.</td>
</tr>
<tr>
<td><strong>Sales</strong></td>
<td>Sales relate to the sale of all products (both prescription and retail) for which goods were purchased at wholesale for the purpose of re-sale at a profit.</td>
</tr>
<tr>
<td><strong>Services income</strong></td>
<td>Includes government payments such as rural allowances, trade rebates, discounts, commissions, agency fees, dividends and disposal of assets are excluded.</td>
</tr>
<tr>
<td><strong>Scheduled medicines</strong></td>
<td>Pharmaceutical products that are only available from a pharmacy because of the potency and safety profile of the medicine.</td>
</tr>
<tr>
<td><strong>Shopping strip</strong></td>
<td>A shopping strip is where shops are arranged in a row with a footpath in front of the shop. There are usually multiple landlords.</td>
</tr>
<tr>
<td><strong>Small shopping centre</strong></td>
<td>A small shopping centre typically incorporates at least one full time discount department store, a major supermarket and at least 40 specialty shops.</td>
</tr>
<tr>
<td><strong>Total centre area retail</strong></td>
<td>The aggregation of all lettable areas in a shopping centre retail, commercial and miscellaneous.</td>
</tr>
<tr>
<td><strong>Total centre lettable area</strong></td>
<td>The aggregation of all lettable areas in a shopping centre retail, commercial and miscellaneous.</td>
</tr>
<tr>
<td><strong>Total income</strong></td>
<td>Arrived at by subtracting total expenses and cost of goods sold from total revenue; it refers to the trading profit of the pharmacy which may involve several partners. Percentage shown is of total revenue.</td>
</tr>
<tr>
<td><strong>Total Revenue</strong></td>
<td>The arithmetic total of sales and other income; all expenses are expressed as a percentage of total revenue not sales) since a portion of all expenses is also incurred in earning other income.</td>
</tr>
<tr>
<td><strong>Turnover</strong></td>
<td>Turnover is income that a business receives from its normal business activities. Also referred to as revenue.</td>
</tr>
<tr>
<td><strong>Turnover/Sales Per Square Metre</strong></td>
<td>Sales divided by the total number of square metres of rentable area. May apply to individual stores, groups of stores or the total centre.</td>
</tr>
</tbody>
</table>
# SHOPPING CENTRE CLASSIFICATIONS

<table>
<thead>
<tr>
<th>CLASSIFICATION</th>
<th>DEFINITION</th>
<th>KEY FEATURES</th>
</tr>
</thead>
</table>
| City centre          | Retail premises within an arcade or mall development owned by one company, firm or person and promoted as an entity within a major central business district. The total gross lettable area retail exceeds 1,000 square metres. | • Dominated by specialty shops  
• Likely to have frontage on a mall or major CBD road  
• Generally do not include supermarkets  
• Often co-exists with large department stores. |
| Super regional centre| A major shopping centre typically incorporating two full line department stores, one or more full line discount department stores, two supermarkets and approximately 250 specialty shops. The total gross lettable area retail exceeds 85,000 square metres. | • One-stop shopping for all needs  
• Comprehensive coverage of the full range of retail needs (including specialised retail), containing a combination of full line department stores, full line discount department stores, supermarkets, services, chain and other specialty retailers  
• Typically includes a number of entertainment and leisure attractions such as cinemas, arcade games and soft play centres  
• Provides a broad range of shopper facilities (car parking, food court) and amenities (rest rooms, seating). |
| Major regional centre| A major shopping centre typically incorporating at least one full line department store, one or more full line discount department stores, one or more supermarkets and approximately 150 specialty shops. The total gross lettable area retail ranges between 50,000 and 85,000 square metres. | • One-stop shopping for all needs  
• Extensive coverage of the full range of retail needs (including specialised retail), containing a combination of full line department stores, full line discount department stores, supermarkets, services, chain and other specialty retailers  
• Typically includes a number of entertainment and leisure attractions such as cinemas, arcade games and soft play centres  
• Provides a broad range of shopper facilities (car parking, food court) and amenities (rest rooms, seating). |
| Regional centre      | A shopping centre typically incorporates one full line department store, a full line discount department store, one or more supermarkets and approximately 100 specialty shops. Total gross lettable area retail ranges between 30,000 and 50,000 square metres. In some instances, all other characteristics being equal, a centre with two full line discount department stores, without a department store, serves as a regional centre. | • Extensive coverage of a broad range of retail needs (including specialised retail), however, not as exhaustive as major regional centres  
• Contains a combination of full line department stores, full line discount department stores, supermarkets, banks, chain and other specialty retailers  
• Provides a broad range of shopper facilities and amenities. |
<table>
<thead>
<tr>
<th>CLASSIFICATION</th>
<th>DEFINITION</th>
<th>KEY FEATURES</th>
</tr>
</thead>
</table>
| Sub-regional centre | A medium sized shopping centre typically incorporating at least one full line discount department store, a major supermarket and approximately 40 specialty shops. Total gross lettable area retail ranges between 10,000 and 30,000 square metres. | • Provides a broad range of sub-regional retail needs  
• Typically dominated by a full line discount department store or major supermarket.                                                                                                                   |
| Neighbourhood centre | A local shopping centre comprising a supermarket and approximately 35 specialty shops. The total gross lettable area retail is less than 10,000 square metres.                                                                 | • Typically located in residential areas  
• Services an immediate residential neighbourhood  
• Usually has extended trading hours  
• Caters for basic day-to-day retail needs.                                                                                                                                 |
| Bulky goods centre  | A medium to large sized shopping centre dominated by bulky goods retailers (furniture, white goods and other home wares), occupying large areas to display merchandise. Typically contain a small number of specialty shops. The total gross lettable area retail is generally greater than 5,000 square metres. | • Generally located adjacent to large regional centres or in non-traditional retail locations (i.e. greenfield sites and industrial areas)  
• Purpose designed, built and operated, generally with a layout of outlets around a central, landscaped area and an overall design and colour theme to promote the appearance of an integrated development. |
| Specialty store     | A non-major retail shop in a centre that specialises in a narrow range of merchandise with an emphasis on product knowledge and customer service. Shops usually range up to 400 square metres.                                      |                                                                                                                                                                                                            |
| Themed centre       | A specialty shopping centre, located primarily in resort areas to cater for specialist tourist needs, which does not normally include a supermarket.                                                                 | • A resort or tourist style development.  
• The size of the centre is not a determining factor.  
• Comprise mainly specialty shops with food courts.                                                                                                                                             |
| Market              | A covered centre of at least 5,000 square metres dominated by food retailing with at least 50 stalls or outlets. It operates on a permanent or irregular basis.                                                      | • Includes areas with refrigeration facilities and air conditioning as well as areas without these facilities.                                                                                           |
| Outlet centre       | A medium to large sized shopping centre which does not normally include a department store, discount department store, or supermarket.                                                                          | • Comprise specialty shops often selling stock at discounted prices including samples, seconds and discontinued lines.                                                                                     |
| Enclosed mall       | A shopping centre that has an enclosed retail area, is air-conditioned and is entered from a surrounding car park that forms part of the property.                                                              |                                                                                                                                                                                                            |
RETAIN LEASING NEGOTIATIONS – BEST PRACTICE

STRATEGIC AND PRACTICAL CONSIDERATIONS

The following are some of the key strategic and practical matters that must be taken into account when considering leasing a premises:

a) Time constraints - Many people seeking to enter into a lease are under time constraints for a number of reasons (for example, the obligation to complete the purchase of a business by the settlement date).

This often limits the options available and interferes with the ability to make correct decisions. Leasing generally involves the following stages which could take anywhere from several weeks to many months to finalise:

• Considering leasing requirements and issues
• Inspection and research of premises
• Obtaining preliminary documentation
• Applying for and obtaining finance
• Obtaining advice
• Negotiating conditions
• Preparation of final documentation
• Fit-out of premises.

What to watch out for

Don't allow yourself to be forced to make decisions or to agree to enter into a lease by a certain time.

• Don't sign any documents which may place obligations on you, occupy the leased premises or pay any deposit monies until full legal and financial advice has been obtained and it is clearly ascertained that the above matters can be dealt with in the required time frame.
• Ensure legal advice is accessed before signing
• Know the negotiation and agreement phases
• Disclosure statement terms

b) Business needs - The type of business will determine what type of premises and facilities will be required, for example:

• Pharmacies will need cold storage, consulting rooms and display space.
• Pharmacies providing gift items or general health products should be in a location with a high level of pedestrian traffic, such as a shopping centre.

What to watch out for

Don't allow yourself to be forced to make decisions or to agree to enter into a lease by a certain time.

• Don't sign any documents which may place obligations on you, occupy the leased premises or pay any deposit monies until full legal and financial advice has been obtained and it is clearly ascertained that the above matters can be dealt with in the required time frame.
• Ensure legal advice is accessed before signing
• Know the negotiation and agreement phases
• Disclosure statement terms

The future directions of your type of business requires consideration. A business which does not consider business trends in leasing could find itself at a competitive disadvantage. For example, it could be argued that with the increasing use of communications technology, a secretarial service could be operated more profitably from home.

• The type of customers and their requirements will also be a factor in assessing the suitability of the premises.
• Some features of the premises may need to reflect the tenant’s physical limitations.

c) Demographics - Demography is the study of human populations and their size, growth distribution, characteristics and change. Demographic indicators include population size, growth rate, distribution, age, gender, marital status, occupation, income, education, race/ethnicity, birth rate and death rate. Demographic indicators can play a crucial role in understanding past trends and preparing for future developments.

Manufacturers, wholesalers and retailers use population data to segment and target the markets for their specific goods and services. Consideration of population data is a useful aid when evaluating the viability of a location for a business.

What to watch out for

To access the information you need from government bodies, you will have to be specific about what you require. For example, if you wish to provide services to families or the aged some relevant indicators would be:

• How many children aged between two and six years age or are school age live in the target area?
• What is the average age and employment status of the population?
• What is their average income and what are the predominant occupations?
• What other services are being provided in the area?

Population data (ABS Census Data) should not be confused with demand. Do not expect that all of the market will buy your goods or use your services.

Population data is only an indication and should be considered together with all other factors.
d) Location - For many businesses, location can be crucial to successful operation. Location must be considered both specifically and generally. Some specific location considerations would be:

- Where in the shopping centre would this type of business do well?
- How visible is this location?
- Are there any competitors in this shopping centre? Are they well established, are there likely to be any others and where will you be located in relation to your competitors?
- Is there a good traffic flow of customers and how accessible is this location for customers?
- How easily can customers get in and out of this shopping centre and is parking readily available?
- How accessible is this location for deliveries and how close are you to your suppliers?
- How well is this location situated to utilise the services being provided by the landlord and paid for by the tenant?
- Are there any obstructions to the flow of pedestrian traffic to the shop? Which entry point are customers likely to use?
- What is the condition of the roads around the location?
- Is there a major anchor tenant, such as a major chain store, which will attract customers and is that major tenant likely to stay?
- How are other businesses in this shopping area performing and are they profitable?
- What facilities are provided for in this location?

Some general considerations would be

- What type of area would suit this kind of business? For example, an upmarket clothing shop would be best located in a high income area or in an exclusive shopping precinct.
- What type of climate suits this business?
- What is your preferred geographical location?
- How far is the business from your home?
- What type of surroundings are necessary to attract customers? For example, a fashion boutique would be suited to a busy area with amenities such as cafés and theatres to attract young people.

What to watch out for

- Future events and trends that may affect the desirability of a location. For example, plans to allow light industrial activity in a restaurant area.
- Past recent events, such as nearby tenants recently vacating or a shopping centre being rearranged.
- The impact of other nearby businesses. For example, a clothes shop would not be ideally placed near a fish shop which may emit smells that deter customers.
- Other external factors such as the type of persons frequenting the area.
- Is the location one that employees can easily get to and will the location be acceptable to current and future staff?

e) Tenancy mix - It is desirable in any group of shops that the mix of tenants is well balanced. The aim is to offer a wide range of products and services to attract customers to the location and enable the participating businesses to trade without having to compete with similar businesses.

What to watch out for

- Many large and small shopping centres rely on large anchor tenants. Often, a major business, such as a national chain store, will attract many customers to an area and benefit other nearby businesses.
- If the major business ceases to trade in that area, this will affect many surrounding businesses. Great care should be taken if you are seeking to rely on large nearby businesses for trade.
- The likelihood of a major business moving should be investigated.
- Sometimes a business may decide to expand and sell products it does not normally sell, which could have a dramatic effect on surrounding businesses.
- The capability of surrounding businesses expanding their range of products and services needs to be ascertained and if a threat exists, then exclusivity should be obtained as a term of the lease.
- However, it does not necessarily follow that a similar business will impact adversely on trade – sometimes the reverse may be true. For example, coffee strips often attract more trade because of the lifestyle and venue attraction.
• You should ensure that in any group of shops where a certain tenancy mix is represented by the landlord or agent, this is actually the case. This is a major consideration in new shopping centres.

• In some situations a landlord may own only one property and not have any control over surrounding businesses (for example, shopping strips).

• In strata title complexes, a landlord may own all the properties, but then sell them over a period of time. This results in the complex being owned by a number of unrelated landlords.

• The new landlords may not be bound to any exclusivity provision or be concerned about tenancy mix, which could result in new competitors being introduced.

• This problem can be dealt with by lease terms which oblige the original landlord to have a term in the contract of sale requiring the purchaser, and any future purchasers, to continue the exclusivity provisions of the lease.

f) Regulatory requirements and authorities - Planning, health, fire, council and other governmental regulatory bodies oversee, regulate and control the conduct of businesses through legislation and regulations. Governmental regulation will, in many instances, determine whether a business can be conducted from a certain location and on what conditions. In most cases, licences from the appropriate authority will need to be obtained to run a business. Many businesses will need to comply with regulations specific to that business.

If you have signed a lease then you are bound to pay the rent and outgoings and perform all of your other obligations. The fact that you are unable to get the required approval, permit or licence does not release you from your obligations under the lease unless the lease provides so.

In most leases the landlord is not obliged to meet the costs of complying with licence and other regulatory requirements whether structural or otherwise.

What to watch out for

• Just because a licence has been granted or a regulation has been complied with previously, this may not necessarily be the current position. You should ensure that all required approvals, licences and permits are able to be transferred to you and renewed in the future.

• Compliance needs to be for the period of the running of your business, in particular the period of your lease.

• A change in zoning may cause a different mix of business in your location which may in turn adversely affect your business.

• A change in the roads in your location (for example road blockage or change of direction) may have an effect on flow of customer traffic to your business.

g) Building Condition - The building or property to be leased will need to be in a condition which enables you to successfully and profitably operate your business. Generally, there is no warranty from the landlord that the premises are fit for the intended purpose and the tenant takes the premises as they find them. There is no obligation on the landlord to fix the building which you lease unless the lease specifically provides so. Once you have signed the lease you are required to pay rent and outgoings and comply with all your other obligations under the lease, irrespective of the suitability of the premises for your business.

What to watch out for

• A building may be inspected at a certain time of the year and appear to be suitable. However, with a change in season, it may become unsuitable. For example, in the winter it may be subject to flooding or in summer it may be too hot and the air-conditioning system may be inadequate.

• There may be hidden defects such as a weakening of the building structure due to termites.

• Making a building suitable for your business may involve alterations to the premises.

• For most leases the tenant is required, at the end of the lease, to reinstate the premises to the condition they were in at the beginning of the lease. This may be expensive and should be taken into account when making a decision on the suitability of the premises.
h) Fit-out of your premise - In many cases, premises will need fixtures, fittings and services in order to enable the tenant to operate the business. Who is to bear the cost of these items will be determined by negotiation and agreement between the tenant and the landlord. Some of the fit-out items to be considered are:

- Shopfront
- Lighting
- Airconditioning
- Floor coverings
- Power points
- Windows
- Security
- Fixtures
- Water supply and waste
- Electrical fittings and submeters
- Painted walls
- Plastered walls
- Telephone
- Signage
- Smoke detectors and fire control systems.

What to watch out for

- The fit-out costs may be a major cost item which should be recovered from the business.
- Fit-out costs should not leave you with insufficient funds to operate your business.
- For those fit-out items that are at your cost, make sure you negotiate as much as possible that these items are your property and can be removed by you when the lease comes to an end.
- Make sure you properly estimate fit-out requirements. A common problem is the underestimating or overestimating of the space required.

Leasing more space than is required for the business will generally result in higher rent and outgoing charges, which will directly affect the profitability of your business.

i) Prevailing Conditions - In making a decision to rent premises for operating a business, it is prudent to consider the prevailing political, government, economic and social conditions. Essentially you should seek to determine whether now is a good time to be leasing property for the purpose of running a business. Some conditions to take into account are:

- The prevailing interest rates, exchange rates, international traveller trends and commercial prices and their impact on your business.
- Whether the Government and council are open to assisting small business in that area. For example, in relation to zoning and health regulations.
- What the community’s and nearby retailers’ views are on that specific shopping centre and your type of business. (For example, there may be groups lobbying to redirect custom away).
- What the present Government’s position is in relation to charges which may be passed on to the tenant by the landlord.
- Whether the management of the shopping centre is sympathetic to the concerns of retailers.
- Whether the management is driven by a ‘hands on’ management team or by a property trust or landlord seeking a high return for its investors.
- The state of the economy. If it is in an unstable state, a long term lease may cause financial hardship or business failure in the future.
- Whether the current market for your business in the location under consideration is strong.

What to watch out for

- Be careful not to place too much emphasis on a single factor.
- Be careful not to rely solely on prevailing conditions and take into account likely future events, trends and developments.
- Do not re-mould the current situation to suit your objectives.
- Be aware of biased information and seek information from a variety of sources.
j) Future Events and Trends - In deciding whether to lease premises, forthcoming events and likely trends should be taken into account. Some relevant matters are whether:

- In the near future, any new shopping centres will open nearby.
- The shopping centre is old and in need of redeveloping and refurbishing. Is this likely to take place during the term of the lease and how will this affect the business? For example, if the shopping centre is redeveloped or refurbished this may necessitate a relocation or a disruption to business trade.
- The shopping centre or premises is likely to be sold and, therefore, subject to a change in policy. This may mean that the premises or shopping centre will be required for other purposes and the lease will not be renewed.
- The local council is planning to build major cultural facilities, government agencies, libraries and tourism and information centres to stimulate economic recovery where your business is located. Alternately, this could happen elsewhere and draw customers away.
- Public transport facilities are going to be relocated (e.g. moving the bus depot away from the area). Are there going to be any road closures or other changes in roads? Is a major employer in the area moving out or downsizing their staff?
- The government is going to amend tenancy legislation which could affect your rights under your lease.

What to watch out for

- Do not assume that information about future events and trends will be disclosed – you will need to make your own enquiries.
- Satisfy yourself that the premises will be able to cope with future changes to your business, which may include a change to the layout and fit-out of the premises.
- When developing your business plan make sure that the business is sustainable over the full term of the lease. The life cycle of the product or service may be less than the lease term which may lead to business failure.
- Assess whether an event, like a major new retail project in the area, will result in an increase in council rates and land taxes.
- Assess any likely technological changes, such as online shopping, and what effect these may have on your business. Will the premises and the terms of the lease have the flexibility to deal with those changes?

k) Relationships - The success of any leasing arrangement is greatly enhanced if there is full cooperation between landlords and tenants. You should ensure that the landlord is someone with whom you will be able to have a good working relationship in the context of your lease. A well negotiated lease will help you foster a good relationship with your landlord.

NEGOTIATION

Negotiation is a process whereby the landlord and tenant come to an agreement on the terms of their lease. Negotiation is an important part of the leasing process. Theoretically, everything is capable of being negotiated. A lease may be presented as standard, but this does not mean it cannot be changed by negotiation. A lease is able to be negotiated in many cases with terms and conditions to suit tenants and landlords. Usually there is more room to negotiate than most potential tenants consider.

What to watch out for

Generally, leases are prepared by the landlord’s solicitor so it is to be expected that the conditions in the document will be acceptable to the landlord but not necessarily acceptable to you. Seek to vary the lease to make it acceptable to your requirements.

The extent to which a landlord will be willing to negotiate will depend on a number of bargaining factors, some of which are:

- The demand for the premises
- Your desirability as a tenant which may include your ability to meet your leasing obligations and your potential to attract clients and other tenants to the location
- The landlord’s financial position
- The future intentions of the landlord in relation to the premises.
It is to your advantage to prepare a case as to why the landlord needs you as a tenant and the benefits for the landlord. For example, your tenancy will cause an increase in customers which will benefit the landlord’s other tenants. Furthermore, your lease, especially if it is long term, will add significantly to the capital value of the building.

Do not expect that the landlord will agree to all your requirements, but ensure you do not go below your bottom line. Be prepared to walk away if the landlord will not at least meet your bottom line.

**Actions to take**

- Before you can be in a position to negotiate, you need to learn and understand about leasing premises and familiarise yourself with all the issues involved in leasing premises.
- Read this report thoroughly and the other reading and research referred to in this report under Further Assistance.
- The terms of your lease are critical to the success of your business and it is essential that you spend time and effort to get it right from the start. Carefully consider and identify your leasing requirements and those needed to make your business a success.
- The following are some items you will need to consider and ascertain your needs for inclusion or exclusion within your lease:
  1. Period of lease
  2. Options to renew
  3. Rent
  4. Operating expenses
  5. Rent review
  6. Assignment
  7. Redevelopment and relocation clauses
  8. Early termination
  9. Permitted use
  10. Competition and exclusivity
  11. Tenancy mix
  12. Further cost items (legal costs, fit-out)
  13. Condition of premises and structural repairs
  14. Repair and maintenance
  15. Option to purchase/first right of refusal
  16. Responsibility of tenants and agents
  17. Fixtures and chattels
  18. Defaulting under lease
  19. Insurance obligations
  20. Availability of services and facilities
  21. Sinking funds
  22. Access
  23. Hours of business
  24. Common areas
  25. Carpark requirements
  26. Destruction clauses
  27. Landlord obligations
  28. Size of premises
  29. Redecoration
  30. Promotional funds
  31. Signage
  32. Security bond
- To assist you in your negotiations, it is useful to break up your requirements into:
  - Those you must have and cannot proceed without.
  - Those that are desirable, will affect your business overall and are worth fighting for.
  - Those that do not overly affect your business and you are willing to compromise on.
  - Those that do not affect your business.
- Establish a bottom line of requirements that represent the minimum you will accept before leasing the premises that meet your business needs.
- You are in a position to negotiate once your needs have been understood and identified. Depending on how comfortable you are with the complexities of leasing you may need to be represented during negotiations.
- Negotiations are normally through an agent acting for the landlord. Initially it is worthwhile discussing your requirements on an informal basis to ascertain the position of the landlord and whether it is worth proceeding to more formal written negotiations.
- It is generally accepted that both parties will seek to get the best lease they can, so do not be afraid of bargaining.
- All negotiations should be on the basis that they are subject to and conditional on the approval of your solicitor and financial adviser.
LEASING MINIMUM STANDARDS AND BEST PRACTICE

The Commonwealth and all States and Territories have agreed on eight key benchmark principles to provide minimum standards for retail tenancy laws.

The eight key principles deal with the following areas:
- Disclosure
- Ratchet clauses
- Relocation costs
- Rent reviews
- Outgoings (auditing and reporting)
- Lease assignment
- Access to turnover figures
- Dispute resolution procedures.

Outlined below are the core lease requirements that are considered to achieve leasing best practice. These best practice requirements incorporate the eight key benchmark principles to provide minimum standards for retail tenancy laws, setting in place a safety net of protections for retail tenants as agreed on by the Commonwealth and all States and Territories.

LEASING BEST PRACTICE

Disclosure

Many tenancy problems are caused because important information is not disclosed. Before entering into a lease, a full disclosure statement should be obtained.

This should include:
- The lease period and options to renew
- The rent and rent review procedures
- Who is to provide the shop fit-out
- Outgoings and other costs, e.g. Legal fees
- Insurance obligations
- Complete details of the building in which the premises are located
- Tenancy mix
- Exclusivity provisions
- Redevelopment and relocation plans
- Number of premises currently leased
- Number of premises unoccupied
- What is to be provided by the landlord
- All details and representations given by the landlord or the landlord’s representatives during negotiations.

Full disclosure will help prevent otherwise unforeseen circumstances that may have severe consequences for the business. All the provisions of the disclosure should be included in the final lease terms (where these have been agreed).

Term of lease

The term of the lease is important. Depending on the circumstances, a long lease may not be suitable. For example, the future success of a newly started business may be uncertain. It may be preferable to have a shorter term with an option or options to renew the lease.

In considering the term and options of a lease, the time required to recover the setup costs and realise on the goodwill of the business must be considered. There should be sufficient time left in the lease to make the sale of the business attractive to prospective purchasers, which means leaving enough time in the term and options of the lease to recover costs and make the required return on investment.

Rent reviews

The rent is generally subject to a review during the term and at renewal of a lease. Both parties should be able to initiate a rent review.

The business must be able to afford proposed rent increases. Rents should not escalate to unsupportable levels. Reviews based on market rent must allow for rent reductions as well as increases.

For a rent review based on market rent, there should be a cheap and effective way to resolve a dispute if there is a disagreement between the parties.

In the case of a rent review dispute, information should be made available to an independent expert to allow a fair determination of market rent.

Relocation costs

Leases often contain clauses which allow a tenant to be relocated (e.g. where there is a redevelopment or refurbishment). Where this is so, the tenant should be adequately compensated and should be no worse off as a result of the relocation.
Tenancy mix
Circumstances may arise where more than one tenant sells the same type of goods, e.g. in a shopping centre. For the viability and success of any business, exclusivity for operating that type of business and selling particular types of goods needs to be carefully considered before entering into the lease.

Outgoings
The landlord’s outgoings (also called operating expenses) which the landlord passes on to the tenant to pay are a major business expense and each specific outgoing needs to be carefully considered as to its acceptability before entering into the lease. Costs such as structural repairs and capital items should be at the landlord’s expense. Any increases in outgoings over the term of the lease need to be taken into account when assessing the lease.

Outgoings should be limited to those from which the leased premises receives a benefit. The lease should also provide for the tenant to have access to invoices and receipts so all outgoing payments can be checked.

Lease assignment
In order to sell and realise on the goodwill of a business, a tenant will generally require the consent of the landlord to an assignment of a lease.

The lease should provide that consent to the assignment will not be unreasonably withheld by the landlord.

Access to turnover figures
Some leases require the tenant to provide turnover figures. Turnover figures should only be supplied in limited circumstances and only where the tenant has agreed.

End of a lease
When a lease term has come to an end and all options to renew the lease (if any) are used up, the tenant does not have the right to remain in the premises. Once a lease has come to an end, the tenant may be required to vacate the leased premises or enter into a new lease with different terms which could include a higher rent.

To help the tenant prepare for the future, a lease should require the landlord to advise the tenant in writing (e.g. 12 months before the lease expires) whether the lease will be renewed and on what conditions, including the term and rent.

Exercise of option
Where a lease provides for an option to renew, most leases state that the option for renewal is to be exercised within a specified time frame and in writing.

It is critical to ensure that if the tenant wishes to exercise the option, that it is exercised correctly and within the agreed timeline otherwise all rights to renewal will be lost. The tenant may be required to vacate the leased premises or enter into a new lease with different conditions, which could include a higher rent.

It is prudent to diarise when an option to renew must be exercised and include early reminders leading up to that date.

Early Determination of Market Rent at Option.
The Pharmacy Guild remains highly proactive in the reviews and administration of Retail Lease legislation in each State and Territory and constantly lobbies for greater transparency and a fairer playing field for members in this area.

One such area is as a result of the recent reviews of legislation in Queensland and New South Wales, being the introduction of the Early Determination of Market Rent at Option. Which affords those members the right to have market rent effectively negotiated and agreed or determined before being bound by the obligations of exercising their option.

This represents an opportunity to leverage the outcome in line with their right over the Landlord’s property and the Guild seeks to have similar rights become effective in legislative reviews around the country as they come due.

As with all matters concerning a lease option or expiry, time is of the essence and members need to be familiar with these rights and timelines.

Suitability of use
Generally, there is no warranty as to the suitability of the premises for a particular business or for the condition of the premises. A tenant should ensure that the business can be operated from the premises to be leased. The zoning and use should be checked with the relevant planning authority and local council.

Where the leased premises are a strata lot, enquiries should be made with the strata company and the strata plan checked for restrictions on use.
Repairs and maintenance

Repairs and maintenance can be a large expense. The responsibility for repairs and maintenance can sometimes lead to disputes, especially where it is unclear whether the cost is for repair or the replacement of a capital item.

In order to avoid disputes, it is useful to specify certain items as being the landlord’s obligation, e.g. roof and air-conditioning repairs.

Other costs

Before entering into a lease, the prospective tenant should consider all the other leasing costs that may be incurred including legal fees, insurance costs, and other establishment costs.

Dispute resolution procedures

The lease should outline procedures to deal with disputes between the landlord and the tenant. Ideally, a landlord and tenant and/or their representatives should discuss any areas of disagreement and find a workable solution that is satisfactory to both parties.

In most cases, a retail tenancy dispute will be considered first by the Small Business Commissioner. If the matter cannot be resolved through the Small Business Commissioner, the matter may be referred to an Administrative Tribunal (AT) for determination.

For other commercial leases, referral to a mediator, including through the Small Business Commissioner could be less costly than the court system.

The Small Business Commissioner provides a range of services in helping the parties resolve their dispute. This includes providing information, advice and guidance together with bringing the parties together for the purpose of resolving the dispute informally, and more formal impartial alternative dispute resolution.

Alternative dispute resolution can:
• Resolve disputes quickly, allowing you to get back to business sooner.
• Get workable business solutions.
• Have greater control over the outcome and feel more satisfied with the result.
• Save on legal costs and time spent preparing for court.

What to watch out for

• Minimum standards will change over time. It is important to keep informed of developments.
• Each lease situation will be different. However, a best practice approach ensures you are on the right track.
• The best practice points outlined above are only some of the many matters that need to be considered when entering into a commercial lease.

HOW TO GET THE BEST DEAL

As a community pharmacy owner your lease is one of the most important contracts you will ever enter into your business. Rent has a huge impact on your business profit and can potentially be the difference between business success and failure. For pharmacy owners setting out to secure a good deal on their lease, the better informed you are, the more empowered you will be in negotiations with the landlord. Preparation and research is required before any landlord meeting.

Remember to:
• Analyse your costs and how they compare to industry benchmarks
• Put time on your side – know key milestones in your lease agreement
• Create positive relationships with the landlord or their agent
• Know the outcome you are seeking
• Talk to other tenants

Be clear on what you want to achieve

Go into discussions with your landlord with a clear picture of what outcome you would like to achieve. It is not just rent that can be negotiated. You may also consider:
• Utilities (electricity, heating, air conditioning, water and sewerage)
• Security
• Cleaning
• Lettable area
• Fit-out and rebranding costs
• Rent reviews
• Marketing levies
• Discounts for early payment of rent
• Renewing the lease early to value add the landlord’s investment in lieu of a rent reduction.
Talk to Other Tenants

Some of the best inside information is from tenants already in a building. Approach your neighbours within the property (specifically those who have just renewed their leases) and ask how things went. What, if anything, did the landlord offer to them to stay? What terms did they agree to? Was the landlord compatible to their requests? What you learn here may surprise you. Use this information wisely in your negotiations/renegotiations, however some Retailers may not be willing to divulge this information as you may obtain better leasing provisions.

Read and understand your lease

If you simply sign the official looking document the landlord or their leasing agent hands you without thoroughly understanding what all the terms mean, you may later discover embedded in the small print are clauses which can trip you up. These may include limitations on your ability to assign the lease, duplicative maintenance charges, site relocation requirements, kick out provisions, etc.

Remember, you are planning to ‘live’ with your landlord for five to ten years, if not longer. You need to know what the small print means. Evaluate all the terms and conditions in your lease to ensure your interests are protected. Know what they mean and the implications on your business. It is possible these terms may eventually affect your bottom line.

Understand the law

An understanding of legislation relevant to your situation as it may regulate your lease. Even if your lease is not regulated by legislation it is a good idea to make sure you are familiar with it as you might wish to negotiate some of the provisions into your commercial lease.

Frame the conversation

Go into discussion with your landlord with a clear picture of what outcome you would like to achieve. Impress on them the impact of government changes to the PBS. Be prepared to state that the financial impacts are significant. Share your ScriptMAP report (or elements of it). Your opening line to your landlord can be, ‘We need to discuss the future viability of my business and changes needed for my pharmacy to manage this risk.’

Introduce others in the Supply Chain

Be prepared to include your wholesaler, brand managers and franchisors into the conversation of arriving at solutions with your landlord. Don’t be surprised if your landlord asks you what assistance your brand/franchisor is providing you as there will be an expectation that the landlord is not the only one involved in sharing the risk and effect from the outcome.

Do not be afraid to ask for changes in the lease agreement

You should keep in mind that there are no set terms in a lease. That means, just like the amount of rent to be paid, everything is negotiable. You should not be surprised to learn that more often than not a landlord will try to find ways to accommodate the concerns of tenants, provided the issues are raised early in the negotiation phase. And why is that? Because the landlord only makes money when space in his or her building is occupied.

Record, Document, Follow Up and Deliver

It goes without saying that you need to take notes, keep an accurate document trail and set effective follow ups from any meeting you have with your landlord. A handy tip is to email/write to the landlord after each meeting confirming the points and views discussed. This will remove any doubt between the parties. Documentation of all your discussions is key – be warned, if you don’t write it down, you won’t be able to prove at a later date that something was actually done, agreed or conceded.

Keep the Dialogue Happening

As part of your ongoing lease management you should conduct a quarterly review of your benchmarks for occupancy cost and turnover per square metre. This will ensure the processes you adopt to increase sales and manage lease costs are delivering improvements. If not, you will need to review with your landlord in order to explore other options for improvements in your pharmacy business to build resilience for your business.

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22 ScriptMAP is available from the Pharmacy Guild of Australia and is a web based tool that provides pharmacy owners with the ability to forecast the significant impact of PBS changes due to price disclosures and other reforms on dispensing income via a personal report based on individual pharmacy dispensing data.
23 Franchisors particular assistance is the provision of marketing plans, branding guidelines, fit-out plans etc for lessors.
EXPLANATORY NOTES

DEFINITION & TERMS - RENT & OUTGOINGS PER SQUARE METRE

RENT DEFINITION

Pharmacy rents are a major cost for all pharmacies. Careful negotiation and consideration of the benefits provided by a particular site must be taken into account when analysing the:

- Total occupancy costs (inc. outgoings)
- The terms of the lease (inc. security of tenure, exclusivity to the centre, escalation or indexation, options, and review periods/methods)
- The resultant share of profits derived by you and your landlord

In the broad terms, what is rent? Rent is the money or ‘consideration’ that the tenant pays a landlord for granting use or occupation of a property.

For a business person or shopping centre owner (or anyone), the rent is a monthly or an annual sum eg. $2,000 per month or $24,000 per annum. Many people say ‘My rent is $200 per square metre’ ($/M²). One should always calculate rent (gross rent with outgoings) back to an annual sum, as it is more relevant and can be related to the level of business (sales) that one can achieve.

OUTGOINGS DEFINITION

In addition to the rent, the tenant will often be responsible for reimbursing the landlord for outgoings payable under the lease, for example rates, use of services and costs of on-going cleaning and day to day repairs and maintenance. The landlord will generally pay for the repair or replacement of certain fixtures, fittings or equipment on the premises caused by fair wear and tear.

However, the above obligations are not standard to all leases and by no means apply to every situation. When negotiating a new lease it is imperative that the obligations of the landlord and the tenant are discussed and clearly reflected within the lease documents so that there is less likelihood of a dispute later on.

The landlord and tenant needs to be very clear on what outgoings are related to the leased premises, who is responsible for the payment of each outgoing and how will it be paid by either party. This must be documented in the lease and should be in plain English to remove any potential dispute. Similarly, the lease should contain provisions to explain if the outgoing costs will be increased in line rental reviews or another mechanism.

OPERATING EXPENSES

All retail businesses are subject to increasing operating expenses due to cost pressures across a range of business inputs. However the operating expenses of pharmacies are high and are more difficult to offset than for other retail businesses. Lessors need to have a clear understanding of pharmacies’ relatively limited ability to increase margins and recover increased costs, including the significant components associated with occupancy.

Salaries and stock are the main expense for pharmacies, reflecting the requirement to employ qualified pharmacists and to provide service and advice with regard to most products sold, as opposed to the customer self-selection or low service models of many other retailers. Governments contract with independent pharmacies as distribution agents for PBS approved medicines and health services. Strong commercial pressures exist to meet the required service standards which generate additional costs which are not typically faced by other retailers.

Rent comprises the second largest expense for pharmacy businesses and has increased substantially in both dollar and percentage terms over the last decade.

For a typical community pharmacy, the cost of goods sold (purchasing medicine and other stock to sell) comprises approximately two-thirds of their sales revenue. The remaining one third, the gross margin, is then required to pay for all operating expenses before a profit can be achieved for the business.

**High stock holding costs have been amplified through the growing inclusion of high-cost medicines on the PBS, further increasing cost/profit ratios.**
### Confidence

-95% and +95%

The estimated population mean for the variable taking account of the sample mean and size, and assuming a 95% statistical confidence in the estimate.

### Mean

Average

The mean is one of several measures of central tendency that statisticians use to indicate the point on the scale of measures where the population is centred. The mean is the average of the scores in the population or sample. Numerically, it equals the sum of the scores divided by the number of scores.

### Median

The median is the score located at the centre of a distribution. If the total number of values in the sample is even, then the median is the mean of the two middle numbers. The median is a useful number in cases where the distribution has very large extreme values which would otherwise skew the data or mean.

### n

Sample number of observations.

### Rent & Outgoings

Total Rent & Outgoings paid by the pharmacy per the lease document and rental invoice for the site.

### Turnover

Annual sales for the pharmacy as reported for the relevant financial year.

### Shopping Centre Classifications

<table>
<thead>
<tr>
<th>Classification</th>
<th>Number of Shops</th>
</tr>
</thead>
<tbody>
<tr>
<td>Isolated</td>
<td>1 to 4 shops</td>
</tr>
<tr>
<td>Strip</td>
<td>5 to 10 shops</td>
</tr>
<tr>
<td>Neighbourhood</td>
<td>10 to 20 shops</td>
</tr>
<tr>
<td>Sub-Regional &amp; Community</td>
<td>20 to 50 shops</td>
</tr>
<tr>
<td>Regional</td>
<td>50 to 100 shops</td>
</tr>
<tr>
<td>Major Regional</td>
<td>100 plus shops</td>
</tr>
</tbody>
</table>
## GLOSSARY

<table>
<thead>
<tr>
<th>Term</th>
<th>Definition</th>
</tr>
</thead>
<tbody>
<tr>
<td>CPI</td>
<td>Consumer price index.</td>
</tr>
<tr>
<td>Cost of goods sold</td>
<td>The amount paid to purchase goods for re-sale, including the cost of shipping and other costs directly related to the purchase of goods.</td>
</tr>
<tr>
<td>Early Determination of Market Rent</td>
<td>Restricted to QLD &amp; NSW for now. QLD refer to Retail Shop Leases Act 1994 Section 27A, NSW refer to Retail Leases Act 1994 section 32.</td>
</tr>
<tr>
<td>EBITA</td>
<td>Earnings before interest, tax, depreciation and amortization EBITA is calculated by taking net profit before tax and adding back the expenses relating to interest, depreciation and amortization. It provides an indication of profitability eliminating the effects of financing and accounting decisions.</td>
</tr>
<tr>
<td>Expense</td>
<td>All expense items, expressed as a percentage of total revenue.</td>
</tr>
<tr>
<td>Front of shop (FOS)</td>
<td>Front of shop (FOS) or retail sales are total sales less dispensary sales.</td>
</tr>
<tr>
<td>Gross lettable area retail (GLAR)</td>
<td>A measure of the amount of retail space within a shopping centre, commercial building or strip centre available for lease. GLAR is the total floor space available for lease measured from the outside walls. GLAR is used for calculating tenancy areas in shopping centres, strip centres, and commercial buildings.</td>
</tr>
<tr>
<td>Gross margin</td>
<td>Gross margin is the income from which operating expenses are paid, and remaining profit derived. Gross margin is calculated by deducting cost of goods sold from sales.</td>
</tr>
<tr>
<td>Gross Margin Plus Other Income</td>
<td>The arithmetic total of the gross margin and other income. Represents the total gross margin from trading.</td>
</tr>
<tr>
<td>GST</td>
<td>Goods and Services Tax</td>
</tr>
<tr>
<td>Large shopping centre</td>
<td>A large shopping centre typically incorporates at least one department store, one or more discount stores, one or more supermarkets and approximately 100 specialty shops.</td>
</tr>
<tr>
<td>Lease</td>
<td>The lease is the document detailing all the terms agreed between the Lessor and the Lessee.</td>
</tr>
<tr>
<td>Lessee</td>
<td>The person or organisation who rents land or property. Also known as the tenant.</td>
</tr>
<tr>
<td>Lessor</td>
<td>The person or organisation who grants a lease. Also known as the landlord or property owner.</td>
</tr>
<tr>
<td>Major tenancy</td>
<td>Tenancies generally greater than 1,000 square metres (GLAR) that occupy the largest space of any single tenancy in the centre and are considered major attractions to the centre by customers.</td>
</tr>
<tr>
<td>Medical centre</td>
<td>A medical centre is an establishment housing a group of doctors offering healthcare services from a single premises.</td>
</tr>
<tr>
<td>Mini Major</td>
<td>All tenants greater than 400sqm not defined as Major, Other Retail or Non Retail. Some pharmacies in shopping centres have a GLAR over 400m2 and hence need to be treated as a Mini Major and not a Speciality Retailer for the purposes of rental and shop fit requirements.</td>
</tr>
<tr>
<td>Moving Annual Turnover (MAT)</td>
<td>Sales for a twelve-month period calculated on a monthly basis. MAT = preceding 12 months sales including the most current available month minus the corresponding month from the previous year.</td>
</tr>
<tr>
<td>Occupancy Cost Ratio</td>
<td>Occupancy costs for the premises divided by the Moving Annual Turnover and expressed as a percentage. Calculated by dividing the tenant’s total occupancy costs into their gross turnover.</td>
</tr>
</tbody>
</table>
### Glossary (Continued)

<table>
<thead>
<tr>
<th>Term</th>
<th>Definition</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Other Income</strong></td>
<td>Income from items which do not involve cost of goods sold, including that derived from Community Pharmacy Agreement programs or professional services. Dividend and rent income, and other such income not connected with the pharmacy's operation are also included here.</td>
</tr>
<tr>
<td><strong>Operating expenses</strong></td>
<td>Expenditure that a business incurs as a result of performing its normal business operations.</td>
</tr>
<tr>
<td><strong>Outgoings</strong></td>
<td>Outgoings are expenses relating to the retail space including, but are not necessarily limited to, rates, strata levies, insurances, land tax, repairs and maintenance, and management fees. Your retail lease may have a special definition and rules about outgoings.</td>
</tr>
<tr>
<td><strong>PBS</strong></td>
<td>Pharmaceutical Benefits Scheme</td>
</tr>
<tr>
<td><strong>Rent</strong></td>
<td>Rent is a periodic payment by a lessee to a lessor for the use of land or property. Rent is shown in this report exclusive of occupancy cost and GST.</td>
</tr>
<tr>
<td><strong>Revenue</strong></td>
<td>Revenue is income that a business receives from its normal business activities. Also known as turnover.</td>
</tr>
<tr>
<td><strong>Salaries and Wages</strong></td>
<td>Includes wages paid to all staff and locums excluding proprietors’ earnings (since the latter are represented by proprietors’ notional salary). Expressed as a percentage of total revenue.</td>
</tr>
<tr>
<td><strong>Sales</strong></td>
<td>Sales relate to the sale of all products (both prescription and retail) for which goods were purchased at wholesale for the purpose of re-sale at a profit.</td>
</tr>
<tr>
<td><strong>Services income</strong></td>
<td>Includes government payments such as rural allowances, trade rebates, discounts, commissions, agency fees, dividends and disposal of assets are excluded.</td>
</tr>
<tr>
<td><strong>Scheduled medicines</strong></td>
<td>Pharmaceutical products that are only available from a pharmacy because of the potency and safety profile of the medicine.</td>
</tr>
<tr>
<td><strong>Shopping strip</strong></td>
<td>A shopping strip is where shops are arranged in a row with a footpath in front of the shop. There are usually multiple landlords.</td>
</tr>
<tr>
<td><strong>Small shopping centre</strong></td>
<td>A small shopping centre typically incorporates at least one full time discount department store, a major supermarket and at least 40 specialty shops.</td>
</tr>
<tr>
<td><strong>Total centre area retail</strong></td>
<td>The aggregation of all lettable areas in a shopping centre retail, commercial and miscellaneous.</td>
</tr>
<tr>
<td><strong>Total centre lettable area</strong></td>
<td>The aggregation of all lettable areas in a shopping centre retail, commercial and miscellaneous.</td>
</tr>
<tr>
<td><strong>Total income</strong></td>
<td>Arrived at by subtracting total expenses and cost of goods sold from total revenue; it refers to the trading profit of the pharmacy which may involve several partners. Percentage shown is of total revenue.</td>
</tr>
<tr>
<td><strong>Total Revenue</strong></td>
<td>The arithmetic total of sales and other income; all expenses are expressed as a percentage of total revenue not sales) since a portion of all expenses is also incurred in earning other income.</td>
</tr>
<tr>
<td><strong>Turnover</strong></td>
<td>Turnover is income that a business receives from its normal business activities. Also referred to as revenue.</td>
</tr>
<tr>
<td><strong>Turnover/Sales Per Square Metre</strong></td>
<td>Sales divided by the total number of square metres of rentable area. May apply to individual stores, groups of stores or the total centre.</td>
</tr>
</tbody>
</table>
# SHOPPING CENTRE CLASSIFICATIONS

<table>
<thead>
<tr>
<th>CLASSIFICATION</th>
<th>DEFINITION</th>
<th>KEY FEATURES</th>
</tr>
</thead>
</table>
| City centre          | Retail premises within an arcade or mall development owned by one company, firm or person and promoted as an entity within a major central business district. The total gross lettable area retail exceeds 1,000 square metres.                                      | • Dominated by specialty shops  
• Likely to have footage on a mall or major CBD road  
• Generally do not include supermarkets  
• Often co-exists with large department stores.                                                                                                                                                                                                                                                                                                                                                           |
| Super regional centre| A major shopping centre typically incorporating two full line department stores, one or more full line discount department stores, two supermarkets and approximately 250 specialty shops. The total gross lettable area retail exceeds 85,000 square metres.                               | • One-stop shopping for all needs  
• Comprehensive coverage of the full range of retail needs (including specialised retail), containing a combination of full line department stores, full line discount department stores, supermarkets, services, chain and other specialty retailers  
• Typically includes a number of entertainment and leisure attractions such as cinemas, arcade games and soft play centres  
• Provides a broad range of shopper facilities (car parking, food court) and amenities (rest rooms, seating).                                                                                                                                                                                                                                      |
| Major regional centre| A major shopping centre typically incorporating at least one full line department store, one or more full line discount department stores, one or more supermarkets and approximately 150 specialty shops. The total gross lettable area retail ranges between 50,000 and 85,000 square metres.                  | • One-stop shopping for all needs  
• Extensive coverage of the full range of retail needs (including specialised retail), containing a combination of full line department stores, full line discount department stores, supermarkets, services, chain and other specialty retailers  
• Typically includes a number of entertainment and leisure attractions such as cinemas, arcade games and soft play centres  
• Provides a broad range of shopper facilities (car parking, food court) and amenities (rest rooms, seating).                                                                                                                                                                                                                                      |
| Regional centre      | A shopping centre typically incorporates one full line department store, a full line discount department store, one or more supermarkets and approximately 100 specialty shops. Total gross lettable area retail ranges between 30,000 and 50,000 square metres. In some instances, all other characteristics being equal, a centre with two full line discount department stores, without a department store, serves as a regional centre. | • Extensive coverage of a broad range of retail needs (including specialised retail), however, not as exhaustive as major regional centres  
• Contains a combination of full line department stores, full line discount department stores, supermarkets, banks, chain and other specialty retailers  
• Provides a broad range of shopper facilities and amenities.                                                                                                                                                                                                                                                                                                                                                       |
<table>
<thead>
<tr>
<th>CLASSIFICATION</th>
<th>DEFINITION</th>
<th>KEY FEATURES</th>
</tr>
</thead>
</table>
| **Sub-regional centre**      | A medium sized shopping centre typically incorporating at least one full line discount department store, a major supermarket and approximately 40 specialty shops. Total gross lettable area retail ranges between 10,000 and 30,000 square metres. | • Provides a broad range of sub-regional retail needs  
• Typically dominated by a full line discount department store or major supermarket.                                                                                                                   |
| **Neighbourhood centre**     | A local shopping centre comprising a supermarket and approximately 35 specialty shops. The total gross lettable area retail is less than 10,000 square metres.                                                       | • Typically located in residential areas  
• Services an immediate residential neighbourhood  
• Usually has extended trading hours  
• Caters for basic day-to-day retail needs.                                                                                                                               |
| **Bulky goods centre**       | A medium to large sized shopping centre dominated by bulky goods retailers (furniture, white goods and other home wares), occupying large areas to display merchandise. Typically contain a small number of specialty shops. The total gross lettable area retail is generally greater than 5,000 square metres in size. | • Generally located adjacent to large regional centres or in non-traditional retail locations (i.e. greenfield sites and industrial areas)  
• Purpose designed, built and operated, generally with a layout of outlets around a central, landscaped area and an overall design and colour theme to promote the appearance of an integrated development. |
| **Specialty store**          | A non-major retail shop in a centre that specialises in a narrow range of merchandise with an emphasis on product knowledge and customer service. Shops usually range up to 400 square metres.                                                         |                                                                                                                                                                                                             |
| **Themed centre**            | A specialty shopping centre, located primarily in resort areas to cater for specialist tourist needs, which does not normally include a supermarket.                                                                 | • A resort or tourist style development.  
• The size of the centre is not a determining factor.  
• Comprise mainly specialty shops with food courts.                                                                                                                         |
| **Market**                   | A covered centre of at least 5,000 square metres dominated by food retailing with at least 50 stalls or outlets. It operates on a permanent or irregular basis.                                                 | • Includes areas with refrigeration facilities and air conditioning as well as areas without these facilities.                                                                                     |
| **Outlet centre**            | A medium to large sized shopping centre which does not normally include a department store, discount department store, or supermarket.                                                                           | • Comprise specialty shops often selling stock at discounted prices including samples, seconds and discontinued lines.                                                                  |
| **Enclosed mall**            | A shopping centre that has an enclosed retail area, is air-conditioned and is entered from a surrounding car park that forms part of the property.                                                               |                                                                                                                                                                                                             |
Acknowledgements

The Pharmacy Guild of Australia would like to acknowledge the support of the following individuals and their organisations whose contributions enabled the preparation of this report.

PHIL CHAPMAN DIRECTOR, LEASE 1
FRANK SIRIANNI, MEDICI CAPITAL

The Pharmacy Rental Report 2019 is an initiative of the Pharmacy Guild of Australia. The project is coordinated by the Health Economics team.

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PRESIDENT’S FOREWORD

Community pharmacy continues to face new challenges in the current business environment while striving to remain competitive and viable. The Pharmacy Guild of Australia is committed to doing all it can to assist our members to flourish in such a volatile and disruptive climate.

The Guild has produced the 2019 Pharmacy Rental Report to help our members, community pharmacy owners as well as aspiring owners.

The report is a useful reference and briefing document which can be utilised to support future rental negotiations. The latest report has been updated to reflect the necessary information required by members to assist them in negotiating new leasing arrangements.

With the model of pharmacy undergoing change, managing the cost of doing business for pharmacy owners remains important and occupancy costs are a key component of this.

Sound commercial leasing arrangements are essential for pharmacy owners. Not only are occupancy costs, including rent, a significant cost but relocating to alternative premises can be costly and disruptive.

Pharmacy owners have a limited ability to pass on fixed underlying costs such as rent due to prices in the industry largely being regulated. However members need to understand what would be reasonable rental costs for a business and this highlights the importance of reports such as the Pharmacy Rental Report undertaken by the Guild to meet your needs.

We encourage owners to use this report to ensure they have a good understanding of rental issues and follow best practice in retail lease negotiations.

Importantly, the report details how to understand your lease, how to prepare for lease negotiations, and strategic lease management.

It is hoped through greater access to information and this support, pharmacy owners will be able to negotiate efficiently to achieve beneficial arrangements.

The Pharmacy Guild of Australia is confident the 2019 Pharmacy Rental Report will assist owners with this task at this key time in our industry.

I thank all those who have had input into this important document, and commend it to Members.

George Tambassis
National President
EXECUTIVE SUMMARY

This report is a guide to the commercial landscape currently facing community pharmacies in relation to their leasing and landlord relationships.

It also puts the case for consideration by landlords of the special conditions and regulations influencing the capacity of community pharmacies to operate as viable businesses in the retail environment. Part One provides context on community pharmacy and rental/lease considerations. Part Two examines key benchmarks and indicators every pharmacy owner should understand and monitor with respect to leases. Part Three provides a detailed checklist of strategic and practical considerations when negotiating leases.

PART ONE

Community pharmacies continue to play a pivotal role in providing primary healthcare and delivering a wide range of services including dispensing prescriptions; distributing pharmacy only and pharmacist only medicines and over-the-counter products; medication management; advice on minor ailments; and preventive care services. At the same time, community pharmacy is practised in a commercial environment – and like other small businesses, the success and viability of the community pharmacy sector depends on the financial performance of these small businesses in the context of the broader pharmaceutical supply chain.

The average revenue per pharmacy is $3.34 million and 71% of revenue is derived from the sale of prescription medicines. The other 29% includes pharmacy professional services, pharmacy only medicines and over-the-counter products. The gross margin (sales less cost of goods sold) is just over $1 million for the average pharmacy and average annual net profit equates to nearly $101,000.

A retail commercial lease, also known as a retail lease, is a legally binding contract that spells out the rights and responsibilities of a tenant and landlord in respect to retail premises. Retail leasing legislation is State-based, which means that the definition of a retail lease differs in each State and Territory.

Community pharmacy tenants are attractive to landlords. Whether located in a large shopping centre or a small strip, community pharmacies are an essential component of any effective tenancy mix and are ultimately high value tenants. Pharmacies draw high foot traffic and repeat visits to retail centres where they are located. An average community pharmacy will dispense 59,747 prescriptions annually, approximating 14 scripts per person in Australia.

After cost of goods sold and wages/salaries, rent is the next largest expense for many pharmacies. For the average pharmacy dispensing 59,747 prescriptions, trading 62 hours per week and with a size of 239 square metres, rent expenses are approximately 5% of sales. Hence community pharmacy owners need to be aware of this important aspect of their business operations, including:

- What to do before signing a lease, such as considering the length of a lease; purposes and restrictions clauses; rent review clauses.
- Rental/leasing costs contained in a lease (from the costs of preparing a lease to costs associated with signage, fixtures and fittings in the leased premise to wear and tear) and who bears these costs.
- Understanding how negotiation of leasing agreements need to be undertaken fairly, with understanding of the particular circumstances in which community pharmacies operate, such as location, competition, customer traffic, presence of prescribing medical practitioners, opening hours, type of pharmacy and the use of broader sales productivity measures to produce benchmarks for occupancy costs.
- Benchmarking of rental/lease costs (rent as a percentage of gross income is a metric often used to keep rental costs in check). In general, businesses with smaller gross profit margins need to maintain lower rent percentages to achieve net profit.
- Legal and regulatory considerations, such as giving a landlord a financial interest in a pharmacy through a turnover rent provision runs counter to established pharmacy regulatory policy. For this reason, pharmacy specific legislation in all Australian States prohibits or restricts turnover rent for pharmacy premises.
PART TWO

Understanding the use of benchmarking of rental/lease costs is critical to ensuring you negotiate a lease that is in your financial interest. Benchmarking can also be used to ascertain the occupancy costs (rent and outgoings) of a similar type of business, in order to achieve an acceptable profit.

There are many benchmarks available for you to consider. The Australian Tax Office (ATO) has developed several performance benchmarks from the information reported on tax returns and activity statements for the 2015–16 financial year, and these are updated each year. The ATO benchmark performance indicator for Rent/ Turnover for the financial year 2015-16 is a range of 3% to 5%. Similarly, the ATO benchmark range for Labour/ Turnover has a range of 9% to 14%.

A report by Medici Capital for the Guild indicates that in 2018:

- Australian community pharmacy average rent and outgoings per square metre (per annum) was $667 (95% confidence interval ranges from $592 to $742) with the average rent as a percentage of turnover at 4.98% (95% confidence interval ranges from 4.41% to 5.55%).
- Rent and outgoings as proportion of turnover remained fairly constant between 2017 and 2018.
- Rental distribution by quartile showed a decreasing range for rent and outgoings per square metre (psm) in dollar terms in 2018 when compared to 2017, indicating a decreasing range of rents paid by pharmacies across all locations. The range for rent and outgoing as a percentage of turnover experienced a shift towards slightly higher values overall.

Moreover, when comparing rental cost increases to the consumer price index (a measure produced by the Australian Bureau of Statistics for consumer inflation) rent costs have increased at a much stronger pace over the past ten years.

Understanding and monitoring these benchmarks and indicators are critical to being aware of market trends and negotiating and holding a lease.

PART THREE

There are various strategic and practical considerations when negotiating leases. While some of these may seem intuitive, together they constitute a checklist of the ‘due diligence’ community pharmacy owners should undertake. A checklist of these includes:

Strategic and practical considerations

- **Time constraints**: many people seeking to enter into a lease are under time constraints and this often limits the options available and interferes with the ability to make correct decisions.
- **Business needs**: the type of business will determine what type of premises and facilities will be required; for example, pharmacies will need cold storage, consulting rooms and display space.
- **Demographics and location**: consideration of demographics is a useful aid when evaluating the viability of a location for a business.
- **Tenancy mix**: in general it is desirable in any group of shops that the mix of tenants is well balanced.
- **Regulatory requirements and authorities**: the myriad of regulations and administering authorities relevant to your business and its location and tenancy can span planning, health, fire, council and other governmental regulations.
- **Building condition and fit-out of your premise**: who is to bear the cost of building upgrades and fit-out costs will be determined by negotiation and agreement between the tenant and the landlord.
- **Prevailing conditions and future trends**: in making a decision to rent premises for operating a business, it is prudent to consider the prevailing political, government, economic and social conditions as well as expectations about future trends.
**Negotiation**

In addition, it is important you consider the science and art of negotiation. A lease may be presented as standard, but this does not mean it cannot be changed by negotiation. A lease is able to be negotiated in many cases with terms and conditions to suit tenants and landlords. Usually there is more room to negotiate than most potential tenants consider.

You are in a position to negotiate once your needs have been understood and identified. Depending on how comfortable you are with the complexities of leasing you may need to be represented during negotiations.

**Leasing minimum standards and best practice**

The Commonwealth and all States and Territories have agreed on eight key benchmark principles to provide minimum standards for retail tenancy laws. The eight key principles deal with the following areas:

- Disclosure
- Ratchet clauses
- Relocation costs
- Rent reviews
- Outgoings (auditing and reporting)
- Lease assignment
- Access to turnover figures
- Dispute resolution procedures.

You should become aware of these principles insofar as they apply in your jurisdiction and particular situation. As a community pharmacy owner your lease is one of the most important contracts you will ever enter into your business. Rent has a huge impact on your business profit and can potentially be the difference between business success and failure. For pharmacy owners setting out to secure a good deal on their lease, the better informed you are, the more empowered you will be in negotiations with the landlord. Preparation and research is required before any landlord meeting. Remember to:

- Analyse your costs and how they compare to industry benchmarks
- Put time on your side – know key milestones in your lease agreement
- Create positive relationships with the landlord or their agent
- Know the outcome you are seeking
- Talk to other tenants.
PART ONE

PHARMACY OVERVIEW

COMMUNITY PHARMACY PROFILE

Community pharmacists own and operate their businesses – forming an integral part of local communities and contributing to local employment and economic activity.

The average revenue per pharmacy is $2.81 million and 66% of revenue is derived from the sale of prescription medicines. The other 34% includes pharmacy professional services, pharmacy only medicines and over-the-counter products. The gross margin (sales less cost of goods sold) is just over $1 million for the average pharmacy and average annual net profit equates to nearly $110,000\(^2\).

Rural pharmacies represent 16% of the total community pharmacies and there is approximately one (1) pharmacy for every 4,236 Australians. The accessibility of community pharmacy is a strong factor underpinning the high regard in which community pharmacy is held.

Community pharmacies continue to play a pivotal role in providing primary healthcare and delivering a wide range of services including dispensing prescriptions; distributing pharmacy only and pharmacist only medicines and over-the-counter products; medication management; advice on minor ailments; and preventive care services. Ultimately, community pharmacies operate to improve the timely access and quality use of medicines in Australia.

At the same time, community pharmacy is practised in a commercial environment – and like other small businesses, the success and viability of the community pharmacy sector depends on the financial performance of these small businesses in the context of the broader pharmaceutical supply chain.

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Rural pharmacies represent 16% of the total community pharmacies and there is approximately one (1) pharmacy for every 4,236 Australians. The accessibility of community pharmacy is a strong factor underpinning the high regard in which community pharmacy is held.

On average, community pharmacies are open 62 hours a week, and are open for an average of 10 hours a day during the week\(^3\).

After cost of goods sold and wages/salaries, rent is the next largest expense for many pharmacies. For the average pharmacy dispensing 57,442 prescriptions, trading 62 hours per week and with a size of 239 square metres, rent expenses are approximately 6% of sales.

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1 PBS Expenditure and Prescriptions 2017-18, Department of Health
2 Guild Digest 2016
3 IBISWorld Industry Report G4271a Pharmacies in Australia 2017
VALUE OF PHARMACY TO LANDLORDS

In any shopping precinct the selection of retail businesses and how they complement each other will determine the effectiveness of the tenancy mix. Whether located in a large shopping centre or a small strip, community pharmacies are an essential component of any effective tenancy mix and are ultimately high value tenants.

The essential goods and services offered by pharmacies as valued health care providers ensure pharmacies regularly draw customers, generating foot traffic in any retail precinct.

The primary product offerings are prescription-only medicines and over-the-counter controlled ‘pharmacist only’ medicines. Provision of ‘pharmacist only medicines’ requires personal counselling by a pharmacist, thereby ensuring a continued stream of consumers, the vast majority of which (94%)\(^4\) will be served/delivered through a community pharmacy. Community pharmacies also offer health care items, cosmetics, toiletries and other items.

Pharmacies draw high foot traffic and repeat visits to retail centres where they are located. An average community pharmacy will dispense 57,442 prescriptions annually\(^5\), approximately 13 scripts for every person in Australia\(^6\).

As the only premises permitted to dispense prescription-only and other restricted medicines, a community pharmacy is essential for retail locations to provide a complete service to customers. High prescription levels range across the demographic spectrum and for those with chronic conditions, visiting a pharmacy is part of their essential shopping routine.

Pharmacists enjoy a highly trusted relationship with their customers. According to a survey conducted by the Institute for Choice for the Pharmacy Guild of Australia\(^7\):

- 89% of consumers trust their local pharmacist either very highly or completely
- 64% of consumers support the principle that professionals should own the business they work in
- Community pharmacies have a clear advantage over supermarkets in terms of trust and quality of service
- Consumers trust their local pharmacist to deliver the medicines they need and have a level of trust in community pharmacy that greatly exceeds their trust in other potential sources of supply.

In absolute terms, the overwhelming majority of survey respondents place a high degree of trust in the ability of their local pharmacy to provide the best service and advice.

PROFESSIONAL HEALTH SERVICES

Based on their position of trust in the community and the skills that pharmacists possess as health professionals, community pharmacies are increasingly operating as primary health care outlets.

Pharmacies also operate as a primary health destination which customers will attend for immediate medical advice and health services\(^8\). Professional services include blood pressure tests, home medication reviews, bowel cancer screenings, weight management programs, ‘Quit’ smoking support, baby and maternal health services, disease screening, medication management and vaccinations.

STABLE, LOW-RISK TENANTS

Historically community pharmacies have held a strong reputation for having a very low risk of failure, with income generated from government payments and consistent demand for pharmacy products and services.

Pharmacies have significant goodwill attached to their business. With the importance of this goodwill to business performance, and the high cost of a new fit-out, pharmacies are traditionally unlikely to relocate premises but instead seek long-term leases, and are thus stable long term tenants.

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\(^4\) IBISWorld Industry Report G4271a Pharmacies in Australia 2017
\(^5\) Approximately 184 scripts per day based upon a 6 day operating cycle
\(^6\) Guild Digest 2016
\(^8\) Increasing the provision of such professional services is being supported by the Australian Government, most recently in the 2017–18 Budget, however providing these services is not without cost.
**EXCLUSIVE LOCATION REGULATIONS**

The current statutory framework for community pharmacies requires that pharmacies be owned and operated by pharmacists, and imposes certain limitations on the location of new pharmacies or the relocation of existing Pharmaceutical Benefits Scheme (PBS) approved pharmacies.

Legislating the supply of pharmaceutical benefits at particular premises will provide an additional source of stability for pharmacy tenants. The Australian Government has passed legislation cementing the ‘location rules’ by amending the relevant sections of the *National Health Act 1953*.

---

**RENTAL / LEASING**

**DEFINITION & REGULATORY CONSIDERATIONS**

A retail commercial lease, also known as a retail lease, is a legally binding contract that spells out the rights and responsibilities of a tenant and landlord in respect to retail premises. Retail leasing legislation is State-based, which means that the definition of a retail lease differs in each State and Territory. As a general rule, if the property being leased has a shop front, is in a shopping centre and/or is mainly used for selling goods or services to the public then the lease of such a property will most likely be considered to be a retail lease.

As far as rent is concerned, ordinary commercial leases can be prepared on a number of bases. For example, rent could be calculated as follows:

- Base rent, no outgoings
- Base rent, plus outgoings
- Base rent, plus a percentage of sales
- Rent review as market review, fixed percentage, based on CPI measure.

The bargaining positions of the landlord and tenant, including each of their size, demand for premises and strength of the market, could determine the rental terms of the commercial lease.

**WHAT IS A REGISTERED LEASE?**

A registered lease is a lease that is registered on the title of a property. In the majority of States, a lease which is for a period of three (3) years or longer must be registered.

A registered lease provides a tenant with additional property rights compared to an unregistered lease.

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10. % of sales may not be compliant in some state and territory legislation for pharmacy ownership (refer to turnover reporting guidelines).
WHAT TO DO BEFORE YOU SIGN A RETAIL LEASE

The landlord is required by law to give the tenant a draft copy of the lease before it is signed. In some States, the landlord is also required to provide disclosure statements and copies of other documents as specified in the relevant legislation.

Before you sign a lease you should always:

• Take time to review the clauses and terms of the lease
• Discuss any contentious matters with the landlord
• Do not make the mistake and assume the leasing terms cannot be negotiated
• Read any relevant legislation
• Talk to someone from your small business association, fair trading office or a small business lawyer
• Talk to a leasing lawyer, if necessary.

PURPOSES AND RESTRICTIONS CLAUSES

You should check the lease to see if there are clauses which restrict your business activity, such as:

• Does the lease restrict certain types of business activity?
• Does it factor in any potential changes which may occur?
• Does it prohibit you from offering certain services?
• How does the lease provide for any ‘permitted use’ changes during the lease term?

RENT REVIEW CLAUSES

You should check to see what the lease says about rent and changes to the rent. The rent clause or clauses may include changes as a result of increases in CPI, market rent reviews and annual increases.

INSURANCE

The lease should spell out whether or not the landlord insures the property and the tenant’s insurance obligations. In any event, you should consider taking out insurance. If you are unsure about your insurance options you should speak to an insurance broker or business lawyer.

WHEN DOES A RETAIL LEASE START?

A retail lease generally starts on the date specified in the lease document, after it is signed by both the tenant and landlord. It may also start before the formal signing of the lease if the tenant takes possession of the premises before signing the lease.

THE LENGTH OF THE LEASE

One of the essential things you should work out from the start is the term of the lease, including whether or not there is an option to renew at the end of the lease and if so, on what terms or can the lease be less than the minimum as required in some States/Territories.

Commercial leases are generally entered into for a period of 3 to 25 years, which includes an initial term and options for the tenant to renew the lease. For example, a 25 year lease would usually be for an initial term of 5 to 10 years followed by successive options of 5 to 10 years each.

COSTS IN RETAIL LEASES

You need to clarify what the lease says about who is responsible for costs, such as:

• Costs of preparing the lease
• Costs of changing the lease
• Signage, fixtures and fittings
• Stamp duty
• Legal fees
• Promotion and advertising
• Cleaning
• Outgoings
• Wear and tear
• Make good (i.e. at the end of the lease returning the property to the condition it was in at the start of the lease)
• GST.
WHAT STATE IS YOUR BUSINESS LOCATED?

There is no national legislation to cover rental/leasing arrangements. Each State/Territory has its own respective legislation (as at November 2017) which is indicated below:

<table>
<thead>
<tr>
<th>STATE</th>
<th>LEGISLATION</th>
</tr>
</thead>
<tbody>
<tr>
<td>VIC</td>
<td>Retail Leases Act 2003</td>
</tr>
<tr>
<td>NSW</td>
<td>Retail Leases Act 1994</td>
</tr>
<tr>
<td>SA</td>
<td>Retail &amp; Commercial Leases Act 1995</td>
</tr>
<tr>
<td>WA</td>
<td>Commercial Tenancy (Retail Shops) Agreement Act 1985</td>
</tr>
<tr>
<td>ACT</td>
<td>Leases (Commercial and Retail) Act 2001</td>
</tr>
<tr>
<td>QLD</td>
<td>Retail Shop Leases Act 1994</td>
</tr>
<tr>
<td>NT</td>
<td>Business Tenancies (Fair Dealings) Act 2003</td>
</tr>
<tr>
<td>TAS</td>
<td>Fair Trading (Code of Practice for Retail Tenancies) Regulations 1998</td>
</tr>
</tbody>
</table>

WHAT IS AN UNFAIR CONTRACT TERM UNDER MY LEASE?

Tenants should also familiarise themselves with the unfair contract terms legislation that came into effect on 12 November 2016. These provisions help to protect small businesses (i.e. 20 employees or less).

If a term would cause a significant imbalance between the rights of the landlord and the tenant, it may be considered unfair. For instance, unfair terms may include clauses that:

- Restrict a tenant’s right to claim compensation from the landlord
- Appoint the landlord as the tenant’s power of attorney if they default on the lease; or
- Terms that allow the landlord to grant an easement over the premises.

More information is available from:

- Australian Consumer and Competition Commission (ACCC)
- Australian Small Business and Family Enterprise Ombudsman (ASBFEO); or
- Small Business Commissioner in each State or Territory.
RENTAL / LEASING COSTS

WHAT PERCENTAGE OF RENT SHOULD YOU PAY ACCORDING TO YOUR BUSINESS’ GROSS INCOME?

Building rent is a common fixed cost for businesses. Like other overhead costs, it is important to invest a reasonable amount in rent to give yourself a chance to earn bottom-line profit. Though specific percentages vary by industry, rent as a percentage of gross income is a metric often used to keep rental costs in check. In general, businesses with smaller gross profit margins need to maintain lower rent percentages to achieve net profit.

RATIO OF ANNUAL RENT TO ANNUAL SALES

The ratio of a business’ annual gross rent to its gross sales receipts is referred to as the company’s occupancy cost ratio. The figure expresses the percentage of the company’s revenue spent on leasing the business premises each year. Occupancy cost ratios need to be considered as part of a bigger picture that includes other expenses, such as staffing, taxes and debt repayments.

OCCUPANCY COST RATIO

A measure of the retail business overall performance is the Occupancy Cost Ratio (OCR = gross rent as a percentage of Retail Sales) and the productivity measure of turnover per square metre. (Noting that retail sales and turnover refers to front of shop sales – excluding dispensary turnover/income).

Calculating the gross occupancy cost ratio of a premises requires dividing the total annual gross rent by gross sales. Gross occupancy = total annual gross rent / annual gross sales.

For example:

If a business pays:
- Rent per year of $24,000
- Annual sales of $125,000
- $24,000 as percentage of $125,000
- The result is 19.2%, which means the business spends 19.2% of its total receipts on rent.

The object of this ratio is to identify the performance of the physical real estate, the net lettable area (NLA measured in square metres) under lease. It should be noted here that to effectively measure the true performance in terms of location, size, access and retail market opportunity, only retail (front of shop sales) should be considered.

This ratio should be evaluated against industry benchmarks to clearly identify the size (m²) requirements of a particular retail business, as one of the key areas of excessive rental and OCR is a premises that is too large for the actual business volumes.

IDEAL LEVEL

There is no ideal level for a business’ occupancy costs because a business’ bottom line is influenced by a number of other factors. If a business’ occupancy costs percentage is in the high teens and it struggles to make a profit, it should consider looking at other premises or discussing options with the landlord. If a business doesn’t do well despite the fact it pays low occupancy costs, it may consider moving into more expensive premises that will attract more customers.

LOW OCCUPANCY COSTS

A business that has low occupancy costs is better placed to withstand economic volatility and rising supplier prices and staffing costs. A low rent-to-sales ratio, however, isn’t necessarily a sign that a business pays a low rent to its landlord. Although prime retail space in malls and on busy shopping streets is expensive when compared to smaller premises on the outskirts of towns, the increased footfall and higher level of passing customers can more than compensate for more costly rent.

HIGH OCCUPANCY COSTS

If a business’ occupancy costs are too high, then asking the landlord for a reduction in rent is an option. Looking into the landlord’s circumstances before making an approach is wise, though, if the landlord has other unoccupied retail space and the business can obtain a less expensive deal elsewhere, then the business’ representatives could state that the business will have to move unless the rent is cut. Lease reductions can be anywhere from 5% to 50% when the retail sector suffers a significant downturn.

By analysing the ratios of OCR and turnover/m² and comparing with industry benchmarks, more efficient use of real estate under lease and better decision making and negotiating of commercial lease terms can be achieved.
SETTING PHARMACY RENTS

Negotiation of leasing agreements need to be undertaken fairly, with understanding of the particular circumstances in which community pharmacies operate.

ESTABLISHMENT COSTS

Pharmacies require a large amount of capital to establish, through purchase of approval number, store fit-out and establishment of a client base.

Fit-out cost is an expense which must be considered as part of the occupancy costs of a pharmacy.

Pharmacy fit-out costs can range between $1,250 and $1,750 per square metre. Based on this sample, the median pharmacy with a size of 214.5 square metres could invest between $267,500 and $374,500 on a shop refit. In a community setting (i.e. strip shopping centre), it is expected that the pharmacy could be required to be updated approximately once every 10 years, this is dependent upon lease management including terms and conditions.

In major regional shopping centres, the median pharmacy size is approximately 352 square metres and a pharmacy could typically invest between $440,000 and $616,000. It is not unusual for larger pharmacies to spend in excess of $1 million on shop fit-outs. However, shopping centres may require the fit-out to be updated every 3 to 5 years as part of leasing arrangements.

These costs can be significant with investment required to regularly be made in fit-outs to meet landlord specifications. Whilst fit-out costs are not part of rent, they can be largely driven by landlords and add to the total occupancy costs of pharmacy businesses.

PHARMACY – A DISTINCT CASE

When negotiating leasing arrangements, Guild members should satisfy themselves that any comparative occupancy cost measures provided or referenced by the landlord or his or her agent directly reflect pharmacy only benchmarks.

Shopping Centre Classifications Sales Category

Under Shopping Centre Council of Australia (SCCA) guidelines, community pharmacies are included under the general retail sales group category. This category also includes other retail channels such as giftware, cosmetics, discount variety stores, florist shops, pet shops, toy stores and miscellaneous retail outlets.

The average net lettable area of pharmacy stores is also substantially larger than most specialty stores.

In the collation of sales and rental data by landlords for the purposes of rent setting, pharmacy is collated with cosmetics retailers. This classification skews the averages and has flow on impact for the application of this data when negotiating rents, as stores in the cosmetics channel usually lease smaller premises and pay higher per square metre rates.

SHOPPING CENTRE PHARMACIES

Many pharmacies are located within shopping centres. These pharmacies may be subject to guidelines which affect the types of information requested and thereby lease negotiations.

Sales Reporting Guidelines

In November 2018 the Pharmacy Guild of Australia, Australian Retailers Association, National Retailers Association along with the Shopping Centre Council of Australia endorsed and became signatories to The Reporting of Sales and Occupancy Costs-Retail Industry Code of Practice.

The Code took effect on the 1st January 2019 with a 6 month implementation period to the 30th June 2019. From the 1st July 2019 Landlords will have a mutual obligation where Lessees are contractually required to report sales under a Retail Lease in return share data back with Lessees including sales and traffic and importantly prescribe how they treat this data (particularly when applying GST uplift and retail category collation).
The Code is not intended to supercede any existing State & Territory legislation, however over time it is anticipated that this voluntary Code will be reflected in minimum lease standards nationally.

The main focus of the Code Administrative Committee of which the PGA is a member, is to introduce greater transparency as to how Landlords collate and report sales and occupancy cost data, so as to allow Lessee’s to better align their outcomes and benchmarks when negotiating leases.

It should be clearly noted, and in line with the Pharmacy Guild Guidelines for the Reporting of Sales to Landlords and the 2010 Shopping Centre Guidelines for Sales and Occupancy Cost Reporting that the exclusion of reporting any activity derived from the PBS or Pharmacy only sales is deliberate.

A legacy issue for Pharmacy Guild members is those Pharmacies who continue either deliberately or inadvertently to report PBS and Pharmacy only sales activity.

This single issue should be of concern to all members as it is a major cause of inflated rents for Pharmacy particularly in shopping centres.

Sales Productivity Measures
The SCCA Guidelines set out a number of Sales Productivity Measures, which are used by the property industry to produce industry benchmarks for occupancy costs. These benchmarks are used in property industry publications and reports to drive favourable promotion of the value of retail investments (both new and existing), mainly through the reporting of rental growth and returns for shareholders.

Treatment of GST
One sales productivity measure that has particular impact for community pharmacy is the treatment of GST. A standard property industry practice involves collating sales and occupancy costs that include GST in lessee sales reporting and then excluding GST in the occupancy charges of rent and outgoings etc. This treatment of GST results in occupancy cost measures which reflect a better than actual outcome in favour of the property industry.

HOW MUCH RENT CAN YOU AFFORD TO PAY?
Ultimately the business of pharmacy is no different to other businesses. Each owner needs to understand what the likely revenues are, the margin on those revenues, the costs to be incurred in carrying on business, and the profit that is generated. In addition, the owner will take into account the investment needed to operate the business and then assess whether the return on investment is sufficient.

RENT IS A FIXED COST
Occupancy costs are a fixed cost. Once the lease is signed, the overhead will not vary with turnover but instead will vary according to the terms of the lease. What is the percentage increase in rent, the share of overheads, marketing levies and any other outgoings to which you have agreed? These costs, over the term of the lease, can be relatively easily determined and set out. The challenge for an owner is to ascertain whether the revenues will be sufficient to generate returns that will cover these costs and the cost of doing business and leave a profit that will support the business’ balance sheet.

WHAT IS THE RENT WORTH – TO YOU?
Owners should not confuse the value of the real estate with the capacity of their business to pay the rent. Landlords, like pharmacy owners, are focused on return on investment. The real estate demands an acceptable return and, the landlords will say, the market will pay that return. Whether the business that is operated from that space will be able to afford the return is not an exercise that the landlord will undertake or guarantee. Whilst it is certainly in the landlord’s interest to have a tenant who can pay the rent, the landlord does not guarantee the performance of the space.

Owners should also distinguish between what turnover is needed to pay the rent and what turnover is likely to be generated. Once an owner can assess what the commitment will be to occupancy costs, this outlay will be part of your budget and you can ascertain what turnover is needed to provide a reasonable return on investment. The next step is the most important and difficult one – assessing what turnover is likely to be derived from the space.
BE REALISTIC

There are many factors which will feed into this assessment of rent. Location, competition, customer traffic, presence of prescribing medical practitioners, opening hours and type of pharmacy are just a few things to consider. Owners should consider various scenarios – pessimistic, moderate and optimistic – and see what working capital is needed in each instance to ensure their pharmacy is sustainable.

Owners should use this modelling to identify the daily sales targets needed in order to operate successfully. This will provide an instant target and a guide as to business performance.

Higher rents per square metre will obviously require higher sales targets just to break-even. This is further compounded if a large retail space is being considered.

With falling margins due to PBS reforms and strong competition in the health retail space, compounded by high fit-out costs to meet exacting landlord standards, owners need to be cognisant of the challenges that they face in seeking to achieve high multi-million dollar turnovers to cover costs.

REPORTING TURNOVER FIGURES

Landlords typically use standard form leases which are not specific to pharmacy premises. These standard form leases will often include turnover rent provisions and provisions requiring the supply of turnover figures.

A long standing policy underpinning pharmacy regulation in Australia is that ownership of community pharmacies should remain in the hands of pharmacists. ‘Turnover rent’ is rent calculated in whole or part by reference to the turnover or profits of a business; the amount of rent varies depending on the sales results of the business. In effect, this type of rent gives the landlord a financial interest in the business.

Giving a landlord a financial interest in a pharmacy through a turnover rent provision runs counter to established policy. For this reason, pharmacy specific legislation in all Australian States prohibits or restricts turnover rent for pharmacy premises:

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**FIGURE 1:** State-Territory restrictions on the ‘turnover rent’ provisions

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15 There are currently no restrictions on turnover rent in the Northern Territory and the Australian Capital Territory. Nevertheless, pharmacy owners in the Territories do have a legal right to negotiate rent arrangements with their landlord. Pharmacy owners, just like other retail shop owners, can seek to have a rent clause where rent is calculated on a basis other than turnover.
In leases for pharmacy premises, a turnover rent provision may well be excluded because of legal restrictions on turnover rent. However, the provisions requiring the supply of turnover figures often remain part of the lease. This situation presents an opportunity for landlords to refer to turnover figures when calculating rent.

Although turnover rent is prohibited or restricted in all Australian States, in some jurisdictions a landlord is not prevented from requiring a pharmacy owner to supply turnover figures (through reporting monthly sales results, for example). As a consequence, landlords may attempt to include a clause in a lease which requires pharmacy owners to provide turnover figures even when their lease does not include a turnover rent provision.

Including a turnover rent provision in a lease agreement for a pharmacy premise can result in significant consequences for both the landlord and the pharmacy owner, including financial penalties for the landlord. In some cases, a pharmacy owner’s ability to continue to carry out a pharmacy business at the premises may also be at risk. It is therefore important that members are aware of the prohibitions and restrictions on turnover rent when negotiating a new lease, renewing a lease, exercising an option under a lease or participating in a rent review process under an existing lease.

Members should think carefully before agreeing to supply turnover figures to their landlords. In most cases, agreeing to supply turnover figures will not be in the best interests of the pharmacy owner.

With this information in mind, if members do decide to provide turnover figures to their landlord, they should consider the most appropriate way to report turnover.

One option is to agree with your landlord that you will only report turnover based on sales in the general retail and scheduled non-prescription medicine categories (i.e. excluding sales of prescription medicines). In most (if not all) cases this condition will require an amendment to standard form leases to accommodate pharmacy specific provisions, including an appropriate definition of both ‘turnover’ or ‘gross sales’. Another option is to agree to provide turnover including prescription medicines, but with the exclusion of high cost drugs which artificially inflate turnover figures in relation to gross profit due to the very low margins available to pharmacies for these drugs.

If you have an existing lease that validly requires the provision of turnover figures, you must comply with the terms of that lease. However, you and your landlord could agree to a variation of the lease to accommodate changes in the way turnover is reported.

**FIGURE 2:** State-Territory restrictions on the provision of turnover information

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15  **Turnover Rent and Reporting Turnover to Landlords Pharmacy Guidelines. Pharmacy Guild of Australia, 2012**
RENTAL / LEASING BENCHMARKS

What is a benchmark? A benchmark is comparing one’s business processes and performance metrics to industry best practices from other companies. It is a reference point by which something can be measured and compared against to assist in the decision-making process.

Benchmarking is a useful tool to ensure that credible goals, objectives and directions are set and in deciding whether or not to lease certain premises.

Benchmarking can also be used to ascertain the occupancy costs (rent and outgoings) of a similar type of business, in order to achieve an acceptable profit.

Community pharmacy premises vary in size and in their allocation of floor space.

Rates per square metre vary dramatically by State/Territory and location. Prices vary considerably by the type of location, with pharmacies located in large medical centres and large shopping centres being the most expensive per square metre. Similarly, pharmacies in metropolitan areas pay considerably more per square metre than pharmacies located in non-metropolitan areas.

Consider the location and state of your pharmacy, and whether it is in a metropolitan or non-metropolitan location.

GENERAL BENCHMARKS

PHARMACY MARKET

Pharmacy rents and occupancy costs represent a significant and increasing cost of pharmacy operations. Indeed, after cost of goods sold, it is usually the next highest expense after staffing costs. For some pharmacies the landlord earns more from the pharmacy than its owners do.

Pharmacy often pays a premium rent in most locations despite being a low risk tenant with a keen interest in developing the location and site. In the light of recent PBS Reforms, Price Disclosure and competitive retail environment, pharmacists will increasingly need quantifiable data to confirm suitable ranges for tenancy negotiations.

AUSTRALIAN TAX OFFICE BENCHMARK

The Australian Tax Office (ATO) defines ‘Pharmacy’ as businesses that sell prescription medication, medical accessories and other health care products. They may also sell beauty and personal care products, confectionary and gift items.

The ATO17 has developed several performance benchmarks from the information reported on tax returns and activity statements for the 2015–16 financial year, and these are updated each year. These benchmarks do not apply to businesses that only provide labour and management services to pharmacies.

Cost of sales to turnover is the key benchmark range for this industry – it is likely to be the most accurate when predicting business turnover. If you don’t report cost of sales, or only report a small amount, use total expenses to turnover as your key benchmark range instead.

The ATO benchmark performance indicator for Rent/Turnover for the financial year 2015-16 is a range of 3% to 5%. Similarly, the ATO benchmark range for Labour/Turnover has a range of 9% to 14%.

BENCHMARKS

In 2007, a Medici Capital18 report on Australian community pharmacy average rent and outgoings per square metre (per annum) indicated that the average rent was $544.69 (95% confidence interval ranges from $491 to $599) with the average rent as a percentage of turnover was 4.19% (95% confidence interval ranges from 3.85% to 4.52%).

In 2018, a similar report on Australian average rent and outgoings per square metre (per annum) was $667 (95% confidence interval ranges from $592 to $742) with the average rent as a percentage of turnover being 4.98% (95% confidence interval ranges from 4.41% to 5.55%).

Therefore in 2018, the average rent and outgoings per square (per annum) for community pharmacy has increased by approximately $123.00 with the average rent as a percentage of turnover has increased by 0.79 basis points.

## PHARMACY RENT DATA*

### PHARMACY RENT AND OUTGOINGS PER SQUARE METRE

#### TABLE 1: Rent & Outgoings per square metre per annum – FY2018

<table>
<thead>
<tr>
<th>LOCATION</th>
<th>LOW RANGE</th>
<th>AVERAGE</th>
<th>HIGH RANGE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Metro</td>
<td>$736</td>
<td>$831</td>
<td>$925</td>
</tr>
<tr>
<td>Rural</td>
<td>$264</td>
<td>$337</td>
<td>$409</td>
</tr>
<tr>
<td>All Locations</td>
<td>$592</td>
<td>$667</td>
<td>$742</td>
</tr>
</tbody>
</table>

#### TABLE 2: Rent & Outgoings per square metre per annum – FY2017

<table>
<thead>
<tr>
<th>LOCATION</th>
<th>LOW RANGE</th>
<th>AVERAGE</th>
<th>HIGH RANGE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Metro</td>
<td>$813</td>
<td>$891</td>
<td>$969</td>
</tr>
<tr>
<td>Rural</td>
<td>$328</td>
<td>$391</td>
<td>$454</td>
</tr>
<tr>
<td>All Locations</td>
<td>$671</td>
<td>$732</td>
<td>$792</td>
</tr>
</tbody>
</table>

Compared to FY2017, the average rent and outgoings per square metre experienced a 9.70% decrease across all locations. This decrease was higher for pharmacies located in rural areas (14.8%) than for those in metropolitan areas (6.9%). Distribution of rent and outgoings per square metre is noted to be within a small range for the majority of pharmacies, with small numbers of pharmacies paying very high rents. The presence of a small number of pharmacies with very high rent and outgoings per square metre subsequently tend to distort estimates of the average rent paid by pharmacies.

#### FIGURE 3: Distribution of Rent & Outgoings per square metre - FY2018

![Distribution of Rent & Outgoings per square metre - FY2018](image)

Source: Medici Capital data

*Caution is advised when interpreting the annual change between rates for the benchmark figures in the following tables, due to significant change in sample size for the two periods.*
TABLE 3: Rent & Outgoings as a % of Turnover – FY2018

<table>
<thead>
<tr>
<th>LOCATION</th>
<th>LOW RANGE</th>
<th>AVERAGE</th>
<th>HIGH RANGE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Metro</td>
<td>5.26%</td>
<td>6.02%</td>
<td>6.78%</td>
</tr>
<tr>
<td>Rural</td>
<td>2.42%</td>
<td>2.87%</td>
<td>3.33%</td>
</tr>
<tr>
<td>All Locations</td>
<td>4.41%</td>
<td>4.98%</td>
<td>5.55%</td>
</tr>
</tbody>
</table>

TABLE 4: Rent & Outgoings as a % of Turnover – FY2017

<table>
<thead>
<tr>
<th>LOCATION</th>
<th>LOW RANGE</th>
<th>AVERAGE</th>
<th>HIGH RANGE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Metro</td>
<td>5.69%</td>
<td>6.09%</td>
<td>6.49%</td>
</tr>
<tr>
<td>Rural</td>
<td>2.69%</td>
<td>3.18%</td>
<td>3.66%</td>
</tr>
<tr>
<td>All Locations</td>
<td>4.83%</td>
<td>5.16%</td>
<td>5.50%</td>
</tr>
</tbody>
</table>

Rent and outgoings as proportion of turnover remained fairly constant between 2017 and 2018, with a slight increase for the average pharmacy of 0.18%. This increase was driven by rural pharmacies, with the proportion of turnover consumed by rent and outgoings increasing at the low range whilst decreasing in the high range for metropolitan pharmacies.

FIGURE 4: Distribution of Rent & Outgoings % - FY2018

Source: Medici Capital data
Rental distribution by quartile showed a decreasing range for rent and outgoings per square metre (psm) in dollar terms in 2018 when compared to 2017, indicating a smaller range of rents paid by pharmacies across all locations. The range for rent and outgoings as a percentage of turnover remained reasonably constant, but experienced a shift towards slightly higher values overall.

**PHARMACY RENTAL DISTRIBUTION**

<table>
<thead>
<tr>
<th>QUARTILE ANALYSIS</th>
<th>25%</th>
<th>50%</th>
<th>75%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rent &amp; Outgoings per square metre (PSM) per annum</td>
<td>$277</td>
<td>$537</td>
<td>$847</td>
</tr>
<tr>
<td>Rent &amp; Outgoings % Turnover</td>
<td>2.55%</td>
<td>3.73%</td>
<td>6.03%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>QUARTILE ANALYSIS</th>
<th>25%</th>
<th>50%</th>
<th>75%</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rent &amp; Outgoings per square metre (PSM) per annum</td>
<td>$334</td>
<td>$585</td>
<td>$958</td>
</tr>
<tr>
<td>Rent &amp; Outgoings % Turnover</td>
<td>2.58%</td>
<td>4.18%</td>
<td>6.87%</td>
</tr>
</tbody>
</table>

**TABLE 5: Quartile Analysis Rent & Outgoings – FY2018**

**TABLE 6: Quartile Analysis Rent & Outgoings – FY2017**

**PHARMACY RENT & OUTGOINGS PER SQUARE METRE BY STATE & LOCATION**

<table>
<thead>
<tr>
<th>STATE LOCATION</th>
<th>LOW RANGE</th>
<th>AVERAGE</th>
<th>HIGH RANGE</th>
</tr>
</thead>
<tbody>
<tr>
<td>VIC Metropolitan</td>
<td>$690</td>
<td>$816</td>
<td>$942</td>
</tr>
<tr>
<td>VIC Rural</td>
<td>$217</td>
<td>$287</td>
<td>$358</td>
</tr>
<tr>
<td>QLD Metropolitan</td>
<td>$614</td>
<td>$764</td>
<td>$914</td>
</tr>
<tr>
<td>QLD Rural</td>
<td>$5</td>
<td>$437</td>
<td>$870</td>
</tr>
<tr>
<td>NSW Metropolitan</td>
<td>$823</td>
<td>$1,155</td>
<td>$1,486</td>
</tr>
<tr>
<td>NSW Rural</td>
<td>$214</td>
<td>$433</td>
<td>$652</td>
</tr>
<tr>
<td>Australia Wide</td>
<td>$592</td>
<td>$667</td>
<td>$742</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>STATE LOCATION</th>
<th>LOW RANGE</th>
<th>AVERAGE</th>
<th>HIGH RANGE</th>
</tr>
</thead>
<tbody>
<tr>
<td>VIC Metropolitan</td>
<td>$726</td>
<td>$805</td>
<td>$884</td>
</tr>
<tr>
<td>VIC Rural</td>
<td>$238</td>
<td>$284</td>
<td>$330</td>
</tr>
<tr>
<td>QLD Metropolitan</td>
<td>$662</td>
<td>$950</td>
<td>$1,238</td>
</tr>
<tr>
<td>QLD Rural</td>
<td>$403</td>
<td>$613</td>
<td>$823</td>
</tr>
<tr>
<td>NSW Metropolitan</td>
<td>$1,007</td>
<td>$1,179</td>
<td>$1,351</td>
</tr>
<tr>
<td>NSW Rural</td>
<td>$301</td>
<td>$429</td>
<td>$557</td>
</tr>
<tr>
<td>Australia Wide</td>
<td>$671</td>
<td>$732</td>
<td>$792</td>
</tr>
</tbody>
</table>

**TABLE 7: Rent & Outgoings per square metre per annum – FY2018**

**TABLE 8: Rent & Outgoings per square metre per annum – FY2017**

19 East Coast only.
PHARMACY RENT DATA
(CONTINUED)

PHARMACY RENT & OUTGOINGS PER SQUARE METRE BY SHOPPING CENTRE TYPE

TABLE 9: Rent & Outgoings psm by Shopping Centre Type – FY2018

<table>
<thead>
<tr>
<th>SHOPPING CENTRE TYPE</th>
<th>LOW RANGE</th>
<th>AVERAGE</th>
<th>HIGH RANGE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Isolated</td>
<td>$64</td>
<td>$318</td>
<td>$571</td>
</tr>
<tr>
<td>Strip</td>
<td>$232</td>
<td>$430</td>
<td>$629</td>
</tr>
<tr>
<td>Neighbourhood</td>
<td>$418</td>
<td>$511</td>
<td>$605</td>
</tr>
<tr>
<td>Sub-Regional &amp; Community</td>
<td>$532</td>
<td>$653</td>
<td>$774</td>
</tr>
<tr>
<td>Regional</td>
<td>$444</td>
<td>$636</td>
<td>$827</td>
</tr>
<tr>
<td>Major Regional</td>
<td>$998</td>
<td>$1,356</td>
<td>$1,715</td>
</tr>
<tr>
<td>Medical Centre</td>
<td>$630</td>
<td>$1,055</td>
<td>$1,481</td>
</tr>
<tr>
<td>All Locations</td>
<td>$592</td>
<td>$667</td>
<td>$742</td>
</tr>
</tbody>
</table>

TABLE 10: Rent & Outgoings psm by Shopping Centre Type – FY2017

<table>
<thead>
<tr>
<th>SHOPPING CENTRE TYPE</th>
<th>LOW RANGE</th>
<th>AVERAGE</th>
<th>HIGH RANGE</th>
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</thead>
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<tr>
<td>Isolated</td>
<td>$144</td>
<td>$359</td>
<td>$574</td>
</tr>
<tr>
<td>Strip</td>
<td>$324</td>
<td>$451</td>
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<tr>
<td>Neighbourhood</td>
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<td>$524</td>
<td>$585</td>
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<tr>
<td>Sub-Regional &amp; Community</td>
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<td>Regional</td>
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<td>All Locations</td>
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<td>$792</td>
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</tbody>
</table>

20 Data is based upon Eastern Australia
RENTAL CONTRACTUAL INCREASES VS CONSUMER PRICE INDEX (CPI)

From a landlord’s perspective, rent reviews are an essential component of a commercial lease. Reviewing the rent at specified intervals ensures that the rent keeps pace with current market rates.

The Consumer Price Index (CPI) produced by the Australian Bureau of Statistics (ABS) measures quarterly changes in the price of a ‘basket’ of goods and services which account for a high proportion of expenditure by the CPI population group (i.e. metropolitan households). This ‘fixed basket’ covers a wide range of goods and services. The CPI affects almost all Australians because of the many ways it is used. It is primarily used as a macro-economic indicator by the government and economists to monitor and evaluate levels of inflation in the Australian economy, and for adjusting dollar values of types of fixed payments, such as pensions and contracts.

Rental contractual increases are either a fixed amount or the amount negotiated into the leasing contract to be reviewed each year. Figure 5 below shows the difference in trends between retail rent and CPI, with growth in retail rent outstripping CPI growth by an increasing amount year on year. It should be noted that since 2014, there has been a minimal increase to the CPI rate when compared to the retail rent trend.

FIGURE 5: Comparison of Consumer Price Index and annual increases in retail rent, FY2007–FY2018

Source: Guild Digest 2000 – Guild Digest 2014, ABS 8501.0 June 2014
Note: In 2009 changes to the sampling procedure introduced re-standardised weightings which caused a data anomaly. This result has been standardised in the above figure.

21 Colliers Retail Research and Forecast Report, 2017 and ABS Consumer Price Index 6401.0
TRENDS – RENT PER SQUARE METRE FOR LAST 6 YEARS

The median rent per square metre paid by pharmacies has been increasing in recent years. Data shows that the median rent per square metre has increased by around $150 between 2013 and 2018. Median rents have, however, fallen in the recent year by around $50.00. Figure 6 demonstrates median rent and outgoings per square metre over the previous 7 years. The trend shows overall positive growth during the period.

FIGURE 6: Rent and Outgoings psm, by Financial Year

Source: Medici Capital data
PART THREE

RETAIL LEASING NEGOTIATIONS – BEST PRACTICE

STRATEGIC AND PRACTICAL CONSIDERATIONS

The following are some of the key strategic and practical matters that must be taken into account when considering leasing a premises:

a) Time constraints - Many people seeking to enter into a lease are under time constraints for a number of reasons (for example, the obligation to complete the purchase of a business by the settlement date). This often limits the options available and interferes with the ability to make correct decisions. Leasing generally involves the following stages which could take anywhere from several weeks to many months to finalise:
- Considering leasing requirements and issues
- Inspection and research of premises
- Obtaining preliminary documentation
- Applying for and obtaining finance
- Obtaining advice
- Negotiating conditions
- Preparation of final documentation
- Fit-out of premises.

What to watch out for

Don’t allow yourself to be forced to make decisions or to agree to enter into a lease by a certain time.
- Don’t sign any documents which may place obligations on you, occupy the leased premises or pay any deposit monies until full legal and financial advice has been obtained and it is clearly ascertained that the above matters can be dealt with in the required time frame.
- Ensure legal advice is accessed before signing
- Know the negotiation and agreement phases
- Disclosure statement terms

b) Business needs - The type of business will determine what type of premises and facilities will be required, for example:
- Pharmacies will need cold storage, consulting rooms and display space.
- Pharmacies providing gift items or general health products should be in a location with a high level of pedestrian traffic, such as a shopping centre.

What to watch out for

- The future directions of your type of business requires consideration. A business which does not consider business trends in leasing could find itself at a competitive disadvantage. For example, it could be argued that with the increasing use of communications technology, a secretarial service could be operated more profitably from home.
- The type of customers and their requirements will also be a factor in assessing the suitability of the premises.
- Some features of the premises may need to reflect the tenant’s physical limitations.

c) Demographics - Demography is the study of human populations and their size, growth distribution, characteristics and change. Demographic indicators include population size, growth rate, distribution, age, gender, marital status, occupation, income, education, race/ethnicity, birth rate and death rate. Demographic indicators can play a crucial role in understanding past trends and preparing for future developments.

Manufacturers, wholesalers and retailers use population data to segment and target the markets for their specific goods and services. Consideration of population data is a useful aid when evaluating the viability of a location for a business.

What to watch out for

To access the information you need from government bodies, you will have to be specific about what you require. For example, if you wish to provide services to families or the aged some relevant indicators would be:
- How many children aged between two and six years age or are school age live in the target area?
- What is the average age and employment status of the population?
- What is their average income and what are the predominant occupations?
- What other services are being provided in the area?

Population data (ABS Census Data) should not be confused with demand. Do not expect that all of the market will buy your goods or use your services.

Population data is only an indication and should be considered together with all other factors.
d) Location - For many businesses, location can be crucial to successful operation. Location must be considered both specifically and generally. Some specific location considerations would be:

- Where in the shopping centre would this type of business do well?
- How visible is this location?
- Are there any competitors in this shopping centre? Are they well established, are there likely to be any others and where will you be located in relation to your competitors?
- Is there a good traffic flow of customers and how accessible is this location for customers?
- How easily can customers get in and out of this shopping centre and is parking readily available?
- How accessible is this location for deliveries and how close are you to your suppliers?
- How well is this location situated to utilise the services being provided by the landlord and paid for by the tenant?
- Are there any obstructions to the flow of pedestrian traffic to the shop? Which entry point are customers likely to use?
- What is the condition of the roads around the location?
- Is there a major anchor tenant, such as a major chain store, which will attract customers and is that major tenant likely to stay?
- How are other businesses in this shopping area performing and are they profitable?
- What facilities are provided for in this location?

Some general considerations would be

- What type of area would suit this kind of business? For example, an upmarket clothing shop would be best located in a high income area or in an exclusive shopping precinct.
- What type of climate suits this business?
- What is your preferred geographical location?
- How far is the business from your home?
- What type of surroundings are necessary to attract customers? For example, a fashion boutique would be suited to a busy area with amenities such as cafés and theatres to attract young people.

What to watch out for

- Future events and trends that may affect the desirability of a location. For example, plans to allow light industrial activity in a restaurant area.
- Past recent events, such as nearby tenants recently vacating or a shopping centre being rearranged.
- The impact of other nearby businesses. For example, a clothes shop would not be ideally placed near a fish shop which may emit smells that deter customers.
- Other external factors such as the type of persons frequenting the area.
- Is the location one that employees can easily get to and will the location be acceptable to current and future staff?

e) Tenancy mix - It is desirable in any group of shops that the mix of tenants is well balanced. The aim is to offer a wide range of products and services to attract customers to the location and enable the participating businesses to trade without having to compete with similar businesses.

What to watch out for

- Many large and small shopping centres rely on large anchor tenants. Often, a major business, such as a national chain store, will attract many customers to an area and benefit other nearby businesses.
- If the major business ceases to trade in that area, this will affect many surrounding businesses. Great care should be taken if you are seeking to rely on large nearby businesses for trade.
- The likelihood of a major business moving should be investigated.
- Sometimes a business may decide to expand and sell products it does not normally sell, which could have a dramatic effect on surrounding businesses.
- The capability of surrounding businesses expanding their range of products and services needs to be ascertained and if a threat exists, then exclusivity should be obtained as a term of the lease.
- However, it does not necessarily follow that a similar business will impact adversely on trade – sometimes the reverse may be true. For example, coffee strips often attract more trade because of the lifestyle and venue attraction.
• You should ensure that in any group of shops where a certain tenancy mix is represented by the landlord or agent, this is actually the case. This is a major consideration in new shopping centres.

• In some situations a landlord may own only one property and not have any control over surrounding businesses (for example, shopping strips).

• In strata title complexes, a landlord may own all the properties, but then sell them over a period of time. This results in the complex being owned by a number of unrelated landlords.

• The new landlords may not be bound to any exclusivity provision or be concerned about tenancy mix, which could result in new competitors being introduced.

• This problem can be dealt with by lease terms which oblige the original landlord to have a term in the contract of sale requiring the purchaser, and any future purchasers, to continue the exclusivity provisions of the lease.

f) Regulatory requirements and authorities - Planning, health, fire, council and other governmental regulatory bodies oversee, regulate and control the conduct of businesses through legislation and regulations. Governmental regulation will, in many instances, determine whether a business can be conducted from a certain location and on what conditions. In most cases, licences from the appropriate authority will need to be obtained to run a business. Many businesses will need to comply with regulations specific to that business.

If you have signed a lease then you are bound to pay the rent and outgoings and perform all of your other obligations. The fact that you are unable to get the required approval, permit or licence does not release you from your obligations under the lease unless the lease provides so.

In most leases the landlord is not obliged to meet the costs of complying with licence and other regulatory requirements whether structural or otherwise.

What to watch out for

• Just because a licence has been granted or a regulation has been complied with previously, this may not necessarily be the current position. You should ensure that all required approvals, licences and permits are able to be transferred to you and renewed in the future.

• Compliance needs to be for the period of the running of your business, in particular the period of your lease.

• A change in zoning may cause a different mix of business in your location which may in turn adversely affect your business.

• A change in the roads in your location (for example road blockage or change of direction) may have an effect on flow of customer traffic to your business.

What to watch out for

• A building may be inspected at a certain time of the year and appear to be suitable. However, with a change in season, it may become unsuitable. For example, in the winter it may be subject to flooding or in summer it may be too hot and the air-conditioning system may be inadequate.

• There may be hidden defects such as a weakening of the building structure due to termites.

• Making a building suitable for your business may involve alterations to the premises.

• For most leases the tenant is required, at the end of the lease, to reinstate the premises to the condition they were in at the beginning of the lease. This may be expensive and should be taken into account when making a decision on the suitability of the premises.
h) Fit-out of your premise - In many cases, premises will need fixtures, fittings and services in order to enable the tenant to operate the business. Who is to bear the cost of these items will be determined by negotiation and agreement between the tenant and the landlord. Some of the fit-out items to be considered are:

- Shopfront
- Lighting
- Airconditioning
- Floor coverings
- Power points
- Windows
- Security
- Fixtures
- Water supply and waste
- Electrical fittings and submeters
- Painted walls
- Plastered walls
- Telephone
- Signage
- Smoke detectors and fire control systems.

What to watch out for

- The fit-out costs may be a major cost item which should be recovered from the business.
- Fit-out costs should not leave you with insufficient funds to operate your business.
- For those fit-out items that are at your cost, make sure you negotiate as much as possible that these items are your property and can be removed by you when the lease comes to an end.
- Make sure you properly estimate fit-out requirements. A common problem is the underestimating or overestimating of the space required.

Leasing more space than is required for the business will generally result in higher rent and outgoing charges, which will directly affect the profitability of your business.

i) Prevailing Conditions - In making a decision to rent premises for operating a business, it is prudent to consider the prevailing political, government, economic and social conditions. Essentially you should seek to determine whether now is a good time to be leasing property for the purpose of running a business. Some conditions to take into account are:

- The prevailing interest rates, exchange rates, international traveller trends and commercial prices and their impact on your business.
- Whether the Government and council are open to assisting small business in that area. For example, in relation to zoning and health regulations.
- What the community’s and nearby retailers’ views are on that specific shopping centre and your type of business. (For example, there may be groups lobbying to redirect custom away).
- What the present Government’s position is in relation to charges which may be passed on to the tenant by the landlord.
- Whether the management of the shopping centre is sympathetic to the concerns of retailers.
- Whether the management is driven by a ‘hands on’ management team or by a property trust or landlord seeking a high return for its investors.
- The state of the economy. If it is in an unstable state, a long term lease may cause financial hardship or business failure in the future.
- Whether the current market for your business in the location under consideration is strong.

What to watch out for

- Be careful not to place too much emphasis on a single factor.
- Be careful not to rely solely on prevailing conditions and take into account likely future events, trends and developments.
- Do not re-mould the current situation to suit your objectives.
- Be aware of biased information and seek information from a variety of sources.
j) Future Events and Trends - In deciding whether to lease premises, forthcoming events and likely trends should be taken into account. Some relevant matters are whether:

- In the near future, any new shopping centres will open nearby.
- The shopping centre is old and in need of redeveloping and refurbishing. Is this likely to take place during the term of the lease and how will this affect the business? For example, if the shopping centre is redeveloped or refurbished this may necessitate a relocation or a disruption to business trade.
- The shopping centre or premises is likely to be sold and, therefore, subject to a change in policy. This may mean that the premises or shopping centre will be required for other purposes and the lease will not be renewed.
- The local council is planning to build major cultural facilities, government agencies, libraries and tourism and information centres to stimulate economic recovery where your business is located. Alternately, this could happen elsewhere and draw customers away.
- Public transport facilities are going to be relocated (e.g. moving the bus depot away from the area). Are there going to be any road closures or other changes in roads? Is a major employer in the area moving out or downsizing their staff?
- The government is going to amend tenancy legislation which could affect your rights under your lease.

What to watch out for

- Do not assume that information about future events and trends will be disclosed – you will need to make your own enquiries.
- Satisfy yourself that the premises will be able to cope with future changes to your business, which may include a change to the layout and fit-out of the premises.
- When developing your business plan make sure that the business is sustainable over the full term of the lease. The life cycle of the product or service may be less than the lease term which may lead to business failure.
- Assess whether an event, like a major new retail project in the area, will result in an increase in council rates and land taxes.
- Assess any likely technological changes, such as online shopping, and what effect these may have on your business. Will the premises and the terms of the lease have the flexibility to deal with those changes?

k) Relationships - The success of any leasing arrangement is greatly enhanced if there is full cooperation between landlords and tenants. You should ensure that the landlord is someone with whom you will be able to have a good working relationship in the context of your lease. A well negotiated lease will help you foster a good relationship with your landlord.

NEGOTIATION

Negotiation is a process whereby the landlord and tenant come to an agreement on the terms of their lease. Negotiation is an important part of the leasing process. Theoretically, everything is capable of being negotiated. A lease may be presented as standard, but this does not mean it cannot be changed by negotiation. A lease is able to be negotiated in many cases with terms and conditions to suit tenants and landlords. Usually there is more room to negotiate than most potential tenants consider.

What to watch out for

Generally, leases are prepared by the landlord’s solicitor so it is to be expected that the conditions in the document will be acceptable to the landlord but not necessarily acceptable to you. Seek to vary the lease to make it acceptable to your requirements.

The extent to which a landlord will be willing to negotiate will depend on a number of bargaining factors, some of which are:

- The demand for the premises
- Your desirability as a tenant which may include your ability to meet your leasing obligations and your potential to attract clients and other tenants to the location
- The landlord’s financial position
- The future intentions of the landlord in relation to the premises.
It is to your advantage to prepare a case as to why the landlord needs you as a tenant and the benefits for the landlord. For example, your tenancy will cause an increase in customers which will benefit the landlord’s other tenants. Furthermore, your lease, especially if it is long term, will add significantly to the capital value of the building.

Do not expect that the landlord will agree to all your requirements, but ensure you do not go below your bottom line. Be prepared to walk away if the landlord will not at least meet your bottom line.

**Actions to take**

- Before you can be in a position to negotiate, you need to learn and understand about leasing premises and familiarise yourself with all the issues involved in leasing premises.
- Read this report thoroughly and the other reading and research referred to in this report under Further Assistance.
- The terms of your lease are critical to the success of your business and it is essential that you spend time and effort to get it right from the start. Carefully consider and identify your leasing requirements and those needed to make your business a success.
- The following are some items you will need to consider and ascertain your needs for inclusion or exclusion within your lease:
  1. Period of lease
  2. Options to renew
  3. Rent
  4. Operating expenses
  5. Rent review
  6. Assignment
  7. Redevelopment and relocation clauses
  8. Early termination
  9. Permitted use
  10. Competition and exclusivity
  11. Tenancy mix
  12. Further cost items (legal costs, fit-out)
  13. Condition of premises and structural repairs
  14. Repair and maintenance
  15. Option to purchase/first right of refusal
  16. Responsibility of tenants and agents
  17. Fixtures and chattels
  18. Defaulting under lease
  19. Insurance obligations
  20. Availability of services and facilities
  21. Sinking funds
  22. Access
  23. Hours of business
  24. Common areas
  25. Carpark requirements
  26. Destruction clauses
  27. Landlord obligations
  28. Size of premises
  29. Redecoration
  30. Promotional funds
  31. Signage
  32. Security bond
- To assist you in your negotiations, it is useful to break up your requirements into:
  - Those you must have and cannot proceed without.
  - Those that are desirable, will affect your business overall and are worth fighting for.
  - Those that do not overly affect your business and you are willing to compromise on.
  - Those that do not affect your business.
- Establish a bottom line of requirements that represent the minimum you will accept before leasing the premises that meet your business needs.
- You are in a position to negotiate once your needs have been understood and identified. Depending on how comfortable you are with the complexities of leasing you may need to be represented during negotiations.
- Negotiations are normally through an agent acting for the landlord. Initially it is worthwhile discussing your requirements on an informal basis to ascertain the position of the landlord and whether it is worth proceeding to more formal written negotiations.
- It is generally accepted that both parties will seek to get the best lease they can, so do not be afraid of bargaining.
- All negotiations should be on the basis that they are subject to and conditional on the approval of your solicitor and financial adviser.
LEASING MINIMUM STANDARDS AND BEST PRACTICE

The Commonwealth and all States and Territories have agreed on eight key benchmark principles to provide minimum standards for retail tenancy laws. The eight key principles deal with the following areas:

- Disclosure
- Ratchet clauses
- Relocation costs
- Rent reviews
- Outgoings (auditing and reporting)
- Lease assignment
- Access to turnover figures
- Dispute resolution procedures.

Outlined below are the core lease requirements that are considered to achieve leasing best practice. These best practice requirements incorporate the eight key benchmark principles to provide minimum standards for retail tenancy laws, setting in place a safety net of protections for retail tenants as agreed on by the Commonwealth and all States and Territories.

LEASING BEST PRACTICE

Disclosure

Many tenancy problems are caused because important information is not disclosed. Before entering into a lease, a full disclosure statement should be obtained.

This should include:

- The lease period and options to renew
- The rent and rent review procedures
- Who is to provide the shop fit-out
- Outgoings and other costs, e.g. Legal fees
- Insurance obligations
- Complete details of the building in which the premises are located
- Tenancy mix
- Exclusivity provisions
- Redevelopment and relocation plans
- Number of premises currently leased
- Number of premises unoccupied

- What is to be provided by the landlord
- All details and representations given by the landlord or the landlord’s representatives during negotiations.

Full disclosure will help prevent otherwise unforeseen circumstances that may have severe consequences for the business. All the provisions of the disclosure should be included in the final lease terms (where these have been agreed).

Term of lease

The term of the lease is important. Depending on the circumstances, a long lease may not be suitable. For example, the future success of a newly started business may be uncertain. It may be preferable to have a shorter term with an option or options to renew the lease.

In considering the term and options of a lease, the time required to recover the setup costs and realise on the goodwill of the business must be considered. There should be sufficient time left in the lease to make the sale of the business attractive to prospective purchasers, which means leaving enough time in the term and options of the lease to recover costs and make the required return on investment.

Rent reviews

The rent is generally subject to a review during the term and at renewal of a lease. Both parties should be able to initiate a rent review.

The business must be able to afford proposed rent increases. Rents should not escalate to unsupportable levels. Reviews based on market rent must allow for rent reductions as well as increases.

For a rent review based on market rent, there should be a cheap and effective way to resolve a dispute if there is a disagreement between the parties.

In the case of a rent review dispute, information should be made available to an independent expert to allow a fair determination of market rent.

Relocation costs

Leases often contain clauses which allow a tenant to be relocated (e.g. where there is a redevelopment or refurbishment). Where this is so, the tenant should be adequately compensated and should be no worse off as a result of the relocation.
Tenancy mix
Circumstances may arise where more than one tenant sells the same type of goods, e.g. in a shopping centre. For the viability and success of any business, exclusivity for operating that type of business and selling particular types of goods needs to be carefully considered before entering into the lease.

Outgoings
The landlord’s outgoings (also called operating expenses) which the landlord passes on to the tenant to pay are a major business expense and each specific outgoing needs to be carefully considered as to its acceptability before entering into the lease. Costs such as structural repairs and capital items should be at the landlord’s expense. Any increases in outgoings over the term of the lease need to be taken into account when assessing the lease.

Outgoings should be limited to those from which the leased premises receives a benefit. The lease should also provide for the tenant to have access to invoices and receipts so all outgoing payments can be checked.

Lease assignment
In order to sell and realise on the goodwill of a business, a tenant will generally require the consent of the landlord to an assignment of a lease.

The lease should provide that consent to the assignment will not be unreasonably withheld by the landlord.

Access to turnover figures
Some leases require the tenant to provide turnover figures. Turnover figures should only be supplied in limited circumstances and only where the tenant has agreed.

End of a lease
When a lease term has come to an end and all options to renew the lease (if any) are used up, the tenant does not have the right to remain in the premises. Once a lease has come to an end, the tenant may be required to vacate the leased premises or enter into a new lease with different terms which could include a higher rent.

To help the tenant prepare for the future, a lease should require the landlord to advise the tenant in writing (e.g. 12 months before the lease expires) whether the lease will be renewed and on what conditions, including the term and rent.

Exercise of option
Where a lease provides for an option to renew, most leases state that the option for renewal is to be exercised within a specified time frame and in writing.

It is critical to ensure that if the tenant wishes to exercise the option, that it is exercised correctly and within the agreed timeline otherwise all rights to renewal will be lost. The tenant may be required to vacate the leased premises or enter into a new lease with different conditions, which could include a higher rent.

It is prudent to diarise when an option to renew must be exercised and include early reminders leading up to that date.

Early Determination of Market Rent at Option.
The Pharmacy Guild remains highly proactive in the reviews and administration of Retail Lease legislation in each State and Territory and constantly lobbies for greater transparency and a fairer playing field for members in this area.

One such area is as a result of the recent reviews of legislation in Queensland and New South Wales, being the introduction of the Early Determination of Market Rent at Option. Which affords those members the right to have market rent effectively negotiated and agreed or determined before being bound by the obligations of exercising their option.

This represents an opportunity to leverage the outcome in line with their right over the Landlord’s property and the Guild seeks to have similar rights become effective in legislative reviews around the country as they come due.

As with all matters concerning a lease option or expiry, time is of the essence and members need to be familiar with these rights and timelines.

Suitability of use
Generally, there is no warranty as to the suitability of the premises for a particular business or for the condition of the premises. A tenant should ensure that the business can be operated from the premises to be leased. The zoning and use should be checked with the relevant planning authority and local council.

Where the leased premises are a strata lot, enquiries should be made with the strata company and the strata plan checked for restrictions on use.
Repairs and maintenance

Repairs and maintenance can be a large expense. The responsibility for repairs and maintenance can sometimes lead to disputes, especially where it is unclear whether the cost is for repair or the replacement of a capital item.

In order to avoid disputes, it is useful to specify certain items as being the landlord’s obligation, e.g. roof and air-conditioning repairs.

Other costs

Before entering into a lease, the prospective tenant should consider all the other leasing costs that may be incurred including legal fees, insurance costs, and other establishment costs.

Dispute resolution procedures

The lease should outline procedures to deal with disputes between the landlord and the tenant. Ideally, a landlord and tenant and/or their representatives should discuss any areas of disagreement and find a workable solution that is satisfactory to both parties.

In most cases, a retail tenancy dispute will be considered first by the Small Business Commissioner. If the matter cannot be resolved through the Small Business Commissioner, the matter may be referred to an Administrative Tribunal (AT) for determination.

For other commercial leases, referral to a mediator, including through the Small Business Commissioner could be less costly than the court system.

The Small Business Commissioner provides a range of services in helping the parties resolve their dispute. This includes providing information, advice and guidance together with bringing the parties together for the purpose of resolving the dispute informally, and more formal impartial alternative dispute resolution.

Alternative dispute resolution can:

• Resolve disputes quickly, allowing you to get back to business sooner.
• Get workable business solutions.
• Have greater control over the outcome and feel more satisfied with the result.
• Save on legal costs and time spent preparing for court.

What to watch out for

• Minimum standards will change over time. It is important to keep informed of developments.
• Each lease situation will be different. However, a best practice approach ensures you are on the right track.
• The best practice points outlined above are only some of the many matters that need to be considered when entering into a commercial lease.

HOW TO GET THE BEST DEAL

As a community pharmacy owner your lease is one of the most important contracts you will ever enter into your business. Rent has a huge impact on your business profit and can potentially be the difference between business success and failure. For pharmacy owners setting out to secure a good deal on their lease, the better informed you are, the more empowered you will be in negotiations with the landlord. Preparation and research is required before any landlord meeting.

Remember to:

• Analyse your costs and how they compare to industry benchmarks
• Put time on your side – know key milestones in your lease agreement
• Create positive relationships with the landlord or their agent
• Know the outcome you are seeking
• Talk to other tenants

Be clear on what you want to achieve

Go into discussions with your landlord with a clear picture of what outcome you would like to achieve. It is not just rent that can be negotiated. You may also consider:

• Utilities (electricity, heating, air conditioning, water and sewerage)
• Security
• Cleaning
• Lettable area
• Fit-out and rebranding costs
• Rent reviews
• Marketing levies
• Discounts for early payment of rent
• Renewing the lease early to value add the landlord’s investment in lieu of a rent reduction.
Talk to Other Tenants

Some of the best inside information is from tenants already in a building. Approach your neighbours within the property (specifically those who have just renewed their leases) and ask how things went. What, if anything, did the landlord offer to them to stay? What terms did they agree to? Was the landlord compatible to their requests? What you learn here may surprise you. Use this information wisely in your negotiations/renegotiations, however some Retailers may not be willing to divulge this information as you may obtain better leasing provisions.

Read and understand your lease

If you simply sign the official looking document the landlord or their leasing agent hands you without thoroughly understanding what all the terms mean, you may later discover embedded in the small print are clauses which can trip you up. These may include limitations on your ability to assign the lease, duplicative maintenance charges, site relocation requirements, kick out provisions, etc.

Remember, you are planning to ‘live’ with your landlord for five to ten years, if not longer. You need to know what the small print means. Evaluate all the terms and conditions in your lease to ensure your interests are protected. Know what they mean and the implications on your business. It is possible these terms may eventually affect your bottom line.

Understand the law

An understanding of legislation relevant to your situation as it may regulate your lease. Even if your lease is not regulated by legislation it is a good idea to make sure you are familiar with it as you might wish to negotiate some of the provisions into your commercial lease.

Frame the conversation

Go into discussion with your landlord with a clear picture of what outcome you would like to achieve. Impress on them the impact of government changes to the PBS. Be prepared to state that the financial impacts are significant. Share your ScriptMAP report (or elements of it). Your opening line to your landlord can be, ‘We need to discuss the future viability of my business and changes needed for my pharmacy to manage this risk’.

Introduce others in the Supply Chain

Be prepared to include your wholesaler, brand managers and franchisors into the conversation of arriving at solutions with your landlord. Don’t be surprised if your landlord asks you what assistance your brand/franchisor is providing you as there will be an expectation that the landlord is not the only one involved in sharing the risk and effect from the outcome.

Do not be afraid to ask for changes in the lease agreement

You should keep in mind that there are no set terms in a lease. That means, just like the amount of rent to be paid, everything is negotiable. You should not be surprised to learn that more often than not a landlord will try to find ways to accommodate the concerns of tenants, provided the issues are raised early in the negotiation phase. And why is that? Because the landlord only makes money when space in his or her building is occupied.

Record, Document, Follow Up and Deliver

It goes without saying that you need to take notes, keep an accurate document trail and set effective follow ups from any meeting you have with your landlord. A handy tip is to email/write to the landlord after each meeting confirming the points and views discussed. This will remove any doubt between the parties. Documentation of all your discussions is key – be warned, if you don’t write it down, you won’t be able to prove at a later date that something was actually done, agreed or conceded.

Keep the Dialogue Happening

As part of your ongoing lease management you should conduct a quarterly review of your benchmarks for occupancy cost and turnover per square metre. This will ensure the processes you adopt to increase sales and manage lease costs are delivering improvements. If not, you will need to review with your landlord in order to explore other options for improvements in your pharmacy business to build resilience for your business.

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22 ScriptMAP is available from the Pharmacy Guild of Australia and is a web based tool that provides pharmacy owners with the ability to forecast the significant impact of PBS changes due to price disclosures and other reforms on dispensing income via a personal report based on individual pharmacy dispensing data.

23 Franchisors particular assistance is the provision of marketing plans, branding guidelines, fit-out plans etc for lessee.
EXPLANATORY NOTES

DEFINITION & TERMS - RENT & OUTGOINGS PER SQUARE METRE

RENT DEFINITION

Pharmacy rents are a major cost for all pharmacies. Careful negotiation and consideration of the benefits provided by a particular site must be taken into account when analysing the:

- Total occupancy costs (inc. outgoings)
- The terms of the lease (inc. security of tenure, exclusivity to the centre, escalation or indexation, options, and review periods/methods)
- The resultant share of profits derived by you and your landlord

In the broad terms, what is rent? Rent is the money or ‘consideration’ that the tenant pays a landlord for granting use or occupation of a property.

For a business person or shopping centre owner (or anyone), the rent is a monthly or an annual sum eg. $2,000 per month or $24,000 per annum. Many people say ‘My rent is $200 per square metre’ ($/M²). One should always calculate rent (gross rent with outgoings) back to an annual sum, as it is more relevant and can be related to the level of business (sales) that one can achieve.

OUTGOINGS DEFINITION

In addition to the rent, the tenant will often be responsible for reimbursing the landlord for outgoings payable under the lease, for example rates, use of services and costs of on-going cleaning and day to day repairs and maintenance. The landlord will generally pay for the repair or replacement of certain fixtures, fittings or equipment on the premises caused by fair wear and tear.

However, the above obligations are not standard to all leases and by no means apply to every situation. When negotiating a new lease it is imperative that the obligations of the landlord and the tenant are discussed and clearly reflected within the lease documents so that there is less likelihood of a dispute later on.

The landlord and tenant needs to be very clear on what outgoings are related to the leased premises, who is responsible for the payment of each outgoing and how will it be paid by either party. This must be documented in the lease and should be in plain English to remove any potential dispute. Similarly, the lease should contain provisions to explain if the outgoing costs will be increased in line rental reviews or another mechanism.

OPERATING EXPENSES

All retail businesses are subject to increasing operating expenses due to cost pressures across a range of business inputs. However the operating expenses of pharmacies are high and are more difficult to offset than for other retail businesses. Lessors need to have a clear understanding of pharmacies’ relatively limited ability to increase margins and recover increased costs, including the significant components associated with occupancy.

Salaries and stock are the main expense for pharmacies, reflecting the requirement to employ qualified pharmacists and to provide service and advice with regard to most products sold, as opposed to the customer self-selection or low service models of many other retailers. Governments contract with independent pharmacies as distribution agents for PBS approved medicines and health services. Strong commercial pressures exist to meet the required service standards which generate additional costs which are not typically faced by other retailers.

Rent comprises the second largest expense for pharmacy businesses and has increased substantially in both dollar and percentage terms over the last decade.

For a typical community pharmacy, the cost of goods sold (purchasing medicine and other stock to sell) comprises approximately two-thirds of their sales revenue. The remaining one third, the gross margin, is then required to pay for all operating expenses before a profit can be achieved for the business.

High stock holding costs have been amplified through the growing inclusion of high-cost medicines on the PBS, further increasing cost/profit ratios.
EXPLANATORY NOTES
(CONTINUED)

<table>
<thead>
<tr>
<th>Confidence</th>
<th>-95% and +95%</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>The estimated population mean for the variable taking account of the sample mean and size, and assuming a 95% statistical confidence in the estimate.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Mean</th>
<th>Average</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>The mean is one of several measures of central tendency that statisticians use to indicate the point on the scale of measures where the population is centred. The mean is the average of the scores in the population or sample. Numerically, it equals the sum of the scores divided by the number of scores.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Median</th>
<th>The median is the score located at the centre of a distribution. If the total number of values in the sample is even, then the median is the mean of the two middle numbers. The median is a useful number in cases where the distribution has very large extreme values which would otherwise skew the data or mean.</th>
</tr>
</thead>
<tbody>
<tr>
<td>n</td>
<td>Sample number of observations.</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Rent &amp; Outgoings</th>
<th>Total Rent &amp; Outgoings paid by the pharmacy per the lease document and rental invoice for the site.</th>
</tr>
</thead>
</table>

<table>
<thead>
<tr>
<th>Turnover</th>
<th>Annual sales for the pharmacy as reported for the relevant financial year.</th>
</tr>
</thead>
</table>

<table>
<thead>
<tr>
<th>Shopping Centre Classifications</th>
<th>Isolated</th>
<th>1 to 4 shops</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Strip</td>
<td>5 to 10 shops</td>
</tr>
<tr>
<td></td>
<td>Neighbourhood</td>
<td>10 to 20 shops</td>
</tr>
<tr>
<td></td>
<td>Sub-Regional &amp; Community</td>
<td>20 to 50 shops</td>
</tr>
<tr>
<td></td>
<td>Regional</td>
<td>50 to 100 shops</td>
</tr>
<tr>
<td></td>
<td>Major Regional</td>
<td>100 plus shops</td>
</tr>
</tbody>
</table>
**GLOSSARY**

<table>
<thead>
<tr>
<th>Term</th>
<th>Definition</th>
</tr>
</thead>
<tbody>
<tr>
<td>CPI</td>
<td>Consumer price index.</td>
</tr>
<tr>
<td>Cost of goods sold</td>
<td>The amount paid to purchase goods for re-sale, including the cost of shipping and other costs directly related to the purchase of goods.</td>
</tr>
<tr>
<td>Early Determination of Market Rent</td>
<td>Restricted to QLD &amp; NSW for now. QLD refer to Retail Shop Leases Act 1994 Section 27A, NSW refer to Retail Leases Act 1994 section 32.</td>
</tr>
<tr>
<td>EBITA</td>
<td><em>Earnings before interest, tax, depreciation and amortization</em> EBITA is calculated by taking net profit before tax and adding back the expenses relating to interest, depreciation and amortization. It provides an indication of profitability eliminating the effects of financing and accounting decisions.</td>
</tr>
<tr>
<td>Expense</td>
<td>All expense items, expressed as a percentage of total revenue.</td>
</tr>
<tr>
<td>Front of shop (FOS)</td>
<td><em>Front of shop</em> (FOS) or retail sales are total sales less dispensary sales.</td>
</tr>
<tr>
<td>Gross lettable area retail (GLAR)</td>
<td>A measure of the amount of retail space within a shopping centre, commercial building or strip centre available for lease. GLAR is the total floor space available for lease measured from the outside walls. GLAR is used for calculating tenancy areas in shopping centres, strip centres, and commercial buildings.</td>
</tr>
<tr>
<td>Gross margin</td>
<td><em>Gross margin</em> is the income from which operating expenses are paid, and remaining profit derived. Gross margin is calculated by deducting cost of goods sold from sales.</td>
</tr>
<tr>
<td>Gross Margin Plus Other Income</td>
<td>The arithmetic total of the gross margin and other income. Represents the total gross margin from trading.</td>
</tr>
<tr>
<td>GST</td>
<td>Goods and Services Tax</td>
</tr>
<tr>
<td>Large shopping centre</td>
<td>A large shopping centre typically incorporates at least one department store, one or more discount stores, one or more supermarkets and approximately 100 specialty shops.</td>
</tr>
<tr>
<td>Lease</td>
<td>The lease is the document detailing all the terms agreed between the Lessor and the Lessee.</td>
</tr>
<tr>
<td>Lessee</td>
<td>The person or organisation who rents land or property. Also known as the tenant.</td>
</tr>
<tr>
<td>Lessor</td>
<td>The person or organisation who grants a lease. Also known as the landlord or property owner.</td>
</tr>
<tr>
<td>Major tenancy</td>
<td>Tenancies generally greater than 1,000 square metres (GLAR) that occupy the largest space of any single tenancy in the centre and are considered major attractions to the centre by customers.</td>
</tr>
<tr>
<td>Medical centre</td>
<td>A medical centre is an establishment housing a group of doctors offering healthcare services from a single premises.</td>
</tr>
<tr>
<td>Mini Major</td>
<td>All tenants greater than 400sqm not defined as Major, Other Retail or Non Retail. Some pharmacies in shopping centres have a GLAR over 400m2 and hence need to be treated as a Mini Major and not a Speciality Retailer for the purposes of rental and shop fit requirements.</td>
</tr>
<tr>
<td>Moving Annual Turnover (MAT)</td>
<td>Sales for a twelve-month period calculated on a monthly basis. MAT = preceding 12 months sales including the most current available month minus the corresponding month from the previous year.</td>
</tr>
<tr>
<td>Occupancy Cost Ratio</td>
<td>Occupancy costs for the premises divided by the <em>Moving Annual Turnover</em> and expressed as a percentage. Calculated by dividing the tenant’s total occupancy costs into their gross turnover.</td>
</tr>
</tbody>
</table>
### GLOSSARY (CONTINUED)

<table>
<thead>
<tr>
<th>Term</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Other Income</strong></td>
<td>Income from items which do not involve cost of goods sold, including that derived from Community Pharmacy Agreement programs or professional services. Dividend and rent income, and other such income not connected with the pharmacy’s operation are also included here.</td>
</tr>
<tr>
<td><strong>Operating expenses</strong></td>
<td>Expenditure that a business incurs as a result of performing its normal business operations.</td>
</tr>
<tr>
<td><strong>Outgoings</strong></td>
<td><em>Outgoings</em> are expenses relating to the retail space including, but are not necessarily limited to, rates, strata levies, insurances, land tax, repairs and maintenance, and management fees. Your retail lease may have a special definition and rules about outgoings.</td>
</tr>
<tr>
<td><strong>PBS</strong></td>
<td>Pharmaceutical Benefits Scheme</td>
</tr>
<tr>
<td><strong>Rent</strong></td>
<td>Rent is a periodic payment by a lessee to a lessor for the use of land or property. Rent is shown in this report exclusive of occupancy cost and GST.</td>
</tr>
<tr>
<td><strong>Revenue</strong></td>
<td>Revenue is income that a business receives from its normal business activities. Also known as turnover.</td>
</tr>
<tr>
<td><strong>Salaries and Wages</strong></td>
<td>Includes wages paid to all staff and locums excluding proprietors’ earnings (since the latter are represented by proprietors’ notional salary). Expressed as a percentage of total revenue.</td>
</tr>
<tr>
<td><strong>Services income</strong></td>
<td>Includes government payments such as rural allowances, trade rebates, discounts, commissions, agency fees, dividends and disposal of assets are excluded.</td>
</tr>
<tr>
<td><strong>Scheduled medicines</strong></td>
<td>Pharmaceutical products that are only available from a pharmacy because of the potency and safety profile of the medicine.</td>
</tr>
<tr>
<td><strong>Shopping strip</strong></td>
<td>A <em>shopping strip</em> is where shops are arranged in a row with a footpath in front of the shop. There are usually multiple landlords.</td>
</tr>
<tr>
<td><strong>Small shopping centre</strong></td>
<td>A small shopping centre typically incorporates at least one full time discount department store, a major supermarket and at least 40 specialty shops.</td>
</tr>
<tr>
<td><strong>Total centre area retail</strong></td>
<td>The aggregation of all lettable areas in a shopping centre retail, commercial and miscellaneous.</td>
</tr>
<tr>
<td><strong>Total centre lettable area</strong></td>
<td>The aggregation of all lettable areas in a shopping centre retail, commercial and miscellaneous.</td>
</tr>
<tr>
<td><strong>Total income</strong></td>
<td>Arrived at by subtracting total expenses and cost of goods sold from total revenue; it refers to the trading profit of the pharmacy which may involve several partners. Percentage shown is of total revenue.</td>
</tr>
<tr>
<td><strong>Total Revenue</strong></td>
<td>The arithmetic total of sales and other income; all expenses are expressed as a percentage of total revenue not sales) since a portion of all expenses is also incurred in earning other income.</td>
</tr>
<tr>
<td><strong>Turnover</strong></td>
<td>Turnover is income that a business receives from its normal business activities. Also referred to as revenue.</td>
</tr>
<tr>
<td><strong>Turnover/Sales Per Square Metre</strong></td>
<td>Sales divided by the total number of square metres of rentable area. May apply to individual stores, groups of stores or the total centre.</td>
</tr>
</tbody>
</table>
### SHOPPING CENTRE CLASSIFICATIONS

<table>
<thead>
<tr>
<th>CLASSIFICATION</th>
<th>DEFINITION</th>
<th>KEY FEATURES</th>
</tr>
</thead>
</table>
| City centre             | Retail premises within an arcade or mall development owned by one company, firm or person and promoted as an entity within a major central business district. The total gross lettable area retail exceeds 1,000 square metres. | • Dominated by specialty shops  
• Likely to have frontage on a mall or major CBD road  
• Generally do not include supermarkets  
• Often co-exists with large department stores. |
| Super regional centre   | A major shopping centre typically incorporating two full line department stores, one or more full line discount department stores, two supermarkets and approximately 250 specialty shops. The total gross lettable area retail exceeds 85,000 square metres. | • One-stop shopping for all needs  
• Comprehensive coverage of the full range of retail needs (including specialised retail), containing a combination of full line department stores, full line discount department stores, supermarkets, services, chain and other specialty retailers  
• Typically includes a number of entertainment and leisure attractions such as cinemas, arcade games and soft play centres  
• Provides a broad range of shopper facilities (car parking, food court) and amenities (rest rooms, seating). |
| Major regional centre   | A major shopping centre typically incorporating at least one full line department store, one or more full line discount department stores, one or more supermarkets and approximately 150 specialty shops. The total gross lettable area retail ranges between 50,000 and 85,000 square metres. | • One-stop shopping for all needs  
• Extensive coverage of the full range of retail needs (including specialised retail), containing a combination of full line department stores, full line discount department stores, supermarkets, services, chain and other specialty retailers  
• Typically includes a number of entertainment and leisure attractions such as cinemas, arcade games and soft play centres  
• Provides a broad range of shopper facilities (car parking, food court) and amenities (rest rooms, seating). |
| Regional centre         | A shopping centre typically incorporates one full line department store, a full line discount department store, one or more supermarkets and approximately 100 specialty shops. Total gross lettable area retail ranges between 30,000 and 50,000 square metres. In some instances, all other characteristics being equal, a centre with two full line discount department stores, without a department store, serves as a regional centre. | • Extensive coverage of a broad range of retail needs (including specialised retail), however, not as exhaustive as major regional centres  
• Contains a combination of full line department stores, full line discount department stores, supermarkets, banks, chain and other specialty retailers  
• Provides a broad range of shopper facilities and amenities. |
<table>
<thead>
<tr>
<th>CLASSIFICATION</th>
<th>DEFINITION</th>
<th>KEY FEATURES</th>
</tr>
</thead>
</table>
| Sub-regional centre    | A medium sized shopping centre typically incorporating at least one full line discount department store, a major supermarket and approximately 40 specialty shops. Total gross lettable area retail ranges between 10,000 and 30,000 square metres.                                                                                   | • Provides a broad range of sub-regional retail needs  
• Typically dominated by a full line discount department store or major supermarket.                                                                                                                                                                     |
| Neighbourhood centre   | A local shopping centre comprising a supermarket and approximately 35 specialty shops. The total gross lettable area retail is less than 10,000 square metres.                                                                                                                                                                                                 | • Typically located in residential areas  
• Services an immediate residential neighbourhood  
• Usually has extended trading hours  
• Caters for basic day-to-day retail needs.                                                                                                                                                                                |
| Bulky goods centre      | A medium to large sized shopping centre dominated by bulky goods retailers (furniture, white goods and other home wares), occupying large areas to display merchandise. Typically contain a small number of specialty shops. The total gross lettable area retail is generally greater than 5,000 square metres.                                           | • Generally located adjacent to large regional centres or in non-traditional retail locations (i.e. greenfield sites and industrial areas)  
• Purpose designed, built and operated, generally with a layout of outlets around a central, landscaped area and an overall design and colour theme to promote the appearance of an integrated development. |
| Specialty store         | A non-major retail shop in a centre that specialises in a narrow range of merchandise with an emphasis on product knowledge and customer service. Shops usually range up to 400 square metres.                                                                                                                  |                                                                                                                                                                                                                                    |
| Themed centre           | A specialty shopping centre, located primarily in resort areas to cater for specialist tourist needs, which does not normally include a supermarket.                                                                                                                                                                                                | • A resort or tourist style development.  
• The size of the centre is not a determining factor.  
• Comprise mainly specialty shops with food courts.                                                                                                                                                                                 |
| Market                  | A covered centre of at least 5,000 square metres dominated by food retailing with at least 50 stalls or outlets. It operates on a permanent or irregular basis.                                                                                                                                                                                        | • Includes areas with refrigeration facilities and air conditioning as well as areas without these facilities.                                                                                                                        |
| Outlet centre           | A medium to large sized shopping centre which does not normally include a department store, discount department store, or supermarket.                                                                                                                                                                                                             | • Comprise specialty shops often selling stock at discounted prices including samples, seconds and discontinued lines.                                                                                                             |
| Enclosed mall           | A shopping centre that has an enclosed retail area, is air-conditioned and is entered from a surrounding car park that forms part of the property.                                                                                                                                                                                                 |                                                                                                                                                                                                                                    |