



TAYLOR WOODINGS

## NEWS FLASH

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### Shaken or just stirred?

#### Recent issues affecting the hospitality industry

A wave of regulatory reform has hit the NSW hospitality industry – and it is unlikely that all operators will survive. As such, it is necessary that financiers and investors alike properly understand:

- the nature of the reforms; and
- how they will impact on the cash flow, profitability and future viability of venues.

#### Circumventing the *Smoke-Free Environment Act 2000*

From 2 July 2007, the *Smoke-Free Environment Act 2000* prohibited smoking in indoor public spaces. Almost immediately, hotels and clubs reported an overall decline in gaming revenue – as smokers chose not to gamble in “smoke free” venues.

In response to the situation, many hotels and clubs established “outdoor” gaming spaces targeting patrons who wanted to smoke and gamble at the same time.

The recent decision of McClellan CJ at Common Law in *Dubbo RSL Memorial Club Limited v Steppalt* [2008] NSWSC 965 has, however, cast doubt on the efficacy of such a strategy. In that case, the Court ruled that the club’s “outdoor” gaming space had to be “smoke free” as it did not constitute an outdoor space. Under the Act, smoking can only occur in a public space where **more than** 25% of the ceiling and wall area of the space is exposed to the elements.

Dubbo RSL spent a reported \$4 million constructing an “outdoor” space comprising a covered gaming area and an uncovered drinking area. It argued that those areas collectively constituted a “single public space” of which more than 25% of the ceiling and wall area was exposed to the elements.

The Court, however, rejected this argument and held that the covered gaming area constituted a “single public space” in its own right and had to be smoke free - as less than 25% of the ceiling and wall area was exposed to the elements.

It will be interesting to see how the hospitality industry responds to this judgment. It is estimated that the hospitality sector has spent in excess of \$1 billion constructing “outdoor” gaming areas in NSW alone.

#### More information

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## Changes imposed by the Liquor Act 2007

On another theme, the Liquor Act 2007 has changed the framework for the licensing and regulation of hotels, clubs and other licenced premises across New South Wales. It has been designed with the aim of:

- providing greater flexibility for the industry – in particular restaurants and dare we say, “Melbourne style” wine bars;
- reducing costs - by changing the processes for obtaining a licence and regulating the industry;
- increasing community involvement – especially with respect to changes to license conditions such as extended trading hours;
- ensuring that venues which do not comply with their licensing conditions are penalised.

## Winners and losers

As with most changes, we expect the *Liquor Act* reforms will generate both winners and losers.

In our view:

- the likely winners will be restaurants and small bars who will benefit from the flexibility and cost savings introduced by the Act; and
- the potential losers will be the owners of large licensed premises who may face increased competition and greater community supervision of their trading activities with less opportunity to differentiate their offering to the market.

## Other industry issues

In addition to the regulatory reform discussed above, the hospitality industry also faces further challenges through:

- increased gaming taxes.
- lower sales revenue and higher interest and wage costs.

Those changes (whilst well flagged) have had a debilitating impact on some industry participants causing a number of hotel and club closures across NSW (particularly highly leveraged operators who recently bought at premium prices).

## Our view

As always, quality operators with good venues and appropriate capital structures should survive the current challenges and may even be able to take advantage of existing opportunities.

However, we hold concerns about less experienced operators managing inferior businesses, especially those competing in saturated, regional or seasonal markets and most of all, those with high levels of gearing. Those operators are likely to experience trading difficulties and in the long run may be unable meet interest repayments and/or generate satisfactory rates of return on their investment.



## How can Taylor Woodings assist?

Taylor Woodings has extensive experience and specialist expertise in the hospitality industry.

In recent times, Taylor Woodings has been appointed as receivers and administrators to a number of licensed hotels and clubs. Taylor Woodings has also provided consulting services to a number of financiers and clubs in relation to various forms of financing (both debt and equity) and operational issues.

Some of our recent roles have involved:

- conducting a pre-lending review of an operator with a chain of licensed premises;
- being appointed as receiver and manager to a number of hotels;
- being appointed voluntary administrator and deed administrator to a number of licensed clubs, which have resulted in the formal restructuring of the clubs' operations and property assets to ensure long term survival of the clubs.

Through our various assignments we have developed:

- a detailed understanding of the legislative and practical issues associated with formal insolvency appointments and commercial issues associated with the industry; and
- an extensive network of contacts in the hospitality industry such as valuers, sales agents, business managers and suppliers who can work with us to ensure that due consideration is given to every aspect of the assignment.

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