Reform of Owners Corporation Legislation – Options Paper

Prudential Investment Company of Australia Pty Ltd (PICA) is a national property and financial services company, focused on the property services industry. PICA was established over 68 years ago with its core industry in body corporate services / strata management where it is the market leader.

PICA group currently manages over 200,000 lots in over 11,000 properties across Victoria, Queensland and New South Wales with an asset value of over $72 billion. BCS is the PICA strata management company in Victoria.

PICA was an active participant in the review of the NSW legislation that lead to two new Acts (and related regulations) that commenced 30 November 2016. PICA has operated since before the first strata scheme registered, the combination of historical experience and contemporary knowledge provide PICA with a unique position from which to respond to this Options Paper.

Our national strata experts have reviewed the options paper and thank Consumer Affairs Victoria for this opportunity to make a submission. For ease of reference we have used the same numbering below as in the Options Paper, page numbers have been used for additional clarity where needed.

If clarification is required on any points made in this submission, please contact our National New Business Advisor, Matilda Halliday on 02 8216 3143 or by email to matilda.halliday@picaust.com.au.

1. Regulation of owners corporation managers

1.1. Licensing versus registration of owners corporation managers

- PICA strongly recommends a full licensing scheme for owners corporation managers. A larger owners corporation often has turn over in excess of $1,000,000 per annum and this requires extensive knowledge, experience and fiduciary responsibility
- We note the comment on page 11 of the Options Paper that for corporations at least one director would be required to be licensed. An alternative would be to adopt a "licensee-in-charge" approach and have such a person be required at each operating location. This provides on the ground oversight of each office, particularly important given the increasing number of franchise operators in the owners corporation management sector. Requiring a director to be licensed does not necessarily ensure a close level of supervision of staff as the director may not work from that location. Requiring a person in the office to undertake this role will increase responsibility and accountability of owners corporations managers
- While the concerns raised on page 11 about additional costs are valid, the additional protection, professionalism and expertise that consumers would have access too is a far greater benefit than any increase in fees
- The transition period of 12 months that is mentioned is appropriate, any longer then the reform has the potential to be ineffective

1.2. Maintaining the knowledge and skills of owners corporation managers

- Any licensing regime must include a requirement for annual professional training that is contemporary and reflective of the changes in owners corporations
- PICA fully endorses the proposal for CPD training similar to that required in NSW

1.3. Unfair terms and termination of management contracts

- Option 3A is the more appropriate option however, clarity is needed about what terms may be *perceived* as unfair compared with those that actually *are* unfair.
- The second dot point on page 15 of the Options Paper is on the surface reasonable however, the apathy that exists with some owners corporations may make it impractical. One option equitable to all stakeholders would be to remove automatic rollover and

allow the committee to agree to a rollover until the next annual general meeting where the matter can be considered by all owners present
- As to question nine, it is reasonable that a fee be payable on termination as a large amount of additional work is required to prepare the books and records for the new managing agent. As long as this is disclosed in the contract of appointment and the rates are not above market there should be no concerns about it.

1.4. Duties and obligations of owners corporation managers
- The matters of conflict of interest and money held on trust need to be considered separately.
- Disclosures of commissions received or potentially received is part of ethical business conduct and should be a requirement. Failure to do so should also result on a report on both the individual and corporate licences concerned
- Committee members should also have obligations about declaration of conflicts of interest/pecuniary benefits (see comments on section 2.3)
- Regarding the first set of dot points on page 17, the first one may not be possible in all cases, especially where the work required is specialist in nature. "Reasonable" is a term that is open to variable interpretations and therefore may cause disputes. The point about provision of bank statements is reasonable but the owners corporation manager should be able to charge a fee for the provision of these (see further comments about access to books and records in 2.2)
- Pooling of trust funds is not a transparent method of financial management. It makes instances of unauthorised removal of funds harder to trace and is not appropriate. PICA's subsidiary BCS holds all owners corporation funds in individual trust accounts, any perception of an additional administrative burden in opening individual accounts is more than out weighted by the additional transparency that is achieved

2. Responsibilities of developers, occupiers and committee members

2.1. Developer' obligations
- While the legislation has just commenced in NSW and the provisions around defects start to apply for construction contracts signed from 1 July 2017 (and therefore are not likely to apply to any owners corporation registered before late 2018 or more likely 2019) the changes introduced in the NSW legislation are the latest example of increasing consumer protection
- How long developers' obligations apply for can reasonably be argued should vary from obligation to obligation. For example, given developers have to pay fees like any other member on the lots they own they should have a say about the appointment of contractors, who committee members are, insurances and the adoption of budgets
- Regarding the setting of lot entitlements, again the NSW legislation provides an independent example – entitlements must be calculated based on market value and a common date and that value must be signed off by a registered valuer
- The NSW legislation also contains consumer protection requiring any fee estimates to be adequate to cover the costs of maintaining the building
- Option 5C seems to be the latest best practice and the most equitable for all stakeholders
- Option 5D, if required, should be an addition to 5C. It is worth noting that the 2% bond regime introduced in NSW while providing consumer protection, will likely result in the cost of the bond being passed onto consumers

2.2. Duties and rights of owners and occupiers
- The seven options listed in 2.2 are of interest, some should be adopted as is, some with additional details/clarifications and some are already covered in legislation

- Option 6A – the inspection of books and records is covered in a sensible way mainly via the NSW and QLD legislation. The change we would suggest is that requests can be made not just in writing and that the fee can be paid at the time of inspection. This is how the inspections work in practice in NSW and QLD. As to the provision of the register to commercial agents, it would not be possible to prevent this if the agent is a lot owner or potential lot owner. If they are not then it should be prohibited with no exception
- Option 6A – invalidation of resolutions and rules. The current Act has no clear process for this and this is required in detail in the new Act
- Option 6B – this option is reasonable in allowing the owners corporation to fulfil their obligation to repair and maintain common property and respecting members privacy
- Option 6C – ensuring a clear position on this question is essential for the owners coronation, for members and for owners corporation managers
- Options 6D and 6E – most state's model rules/by-laws about pets provide two or more options which can be chosen from depending on the nature of the development. It is of note that the new NSW model by-laws no longer had a "no pets" option. As for smoke drift, this is an important issue for the health of occupiers and contractors that attend a property and a clear model by-law would be of benefit. In both cases it will need to be clear if any new model by-law can be applied to an existing property – thereby changing the rules under which an occupier chose to live at the property
  The NSW legislation incorporates three categories of renovations and these amendments have been warmly welcomed by most stakeholders. They provide a good model on how this could be approached for the Victorian market
- Option 6F – it is not at all unusual that rules or by-laws need to be provided to tenants with their agreements. It is generally a condition of such an agreement that tenants comply with the rules, to do so they need to be provided with a copy. This could be done either attached to the agreement or by email or other electronic means
- Option 6G – the placement of responsibility for compliance with the rules is complex. The owners corporation, and the owners corporation's manager as agent, has a "contract" with members and therefore can take action against them. It may be argued that no such "contract" exists with tenants so the owners corporation cannot take action against them only against that lot's owner as a member

2.3. Duties of committee members
- Option 7A is the most appropriate
- As mentioned in our comments on section 1.4, it is *essential* that committee members be required to declare all conflicts of interest, perceived conflicts of interest and any pecuniary interest (direct or indirect). Any such declaration would not automatically remove that committee member from voting on that matter, their authority to vote or not would be best decided by other committee members. Perhaps using the new provisions in the NSW legislation as a model

2.4. Powers of owners corporations regarding community building, water rights and abandoned goods
- Option 8A is an interesting concept however; there is a concern about how such costs would be covered. Inclusion of activities such as clubs and activities in an owners corporation's budget that is charged to all lot owners would not be appropriate. Such costs would be voluntary and an owners corporation would have to set up their own "committee" to manage them. It is notable that there is nothing to prevent a group of owners from setting up their own clubs or activity groups at the moment and a number of properties do this
- Option 8B – more detail is required about the need for such a provision and the resulting obligations on an owners corporation before we can comment on this
- Option 8C – this is an absolute requirement for both goods and, in particular, vehicles. The NSW legislation provides comprehensive models on these processes. These

provisions have had significant uptake in NSW in the two weeks since commencement of their new Act

3. Decision-making within owners corporations
   3.1. Voting thresholds and the use of proxies
   - Option 9A – restrictions on the number of proxies one person can hold can be a way to limit proxy farming however, just because one person holds a large proportion of proxies does not mean they are proxy farming. A number of owners may not be able to attend the meeting but they still want their vote counted so they provide a proxy to a person and this democratic process should not be hindered. A way to allow this but still control proxy farming would be to require owners to write on a proxy form how they wish the bearer to vote on each motion and the bearer must vote that way and can only vote on motions where this instruction is given. We note that you are proposing the same limits on proxies as in NSW. A concern that is already taking place in NSW is where an owner wants their vote counted but they do not know by name another owner so they appoint the chairperson or secretary as their proxy. Appointments to a position rather than a person will lead to a high number of proxies and these should only be valid when voting instructions are provided
     Any limits placed on proxies will need to be hand in hand with a new way of a meeting proceeding where there is a not a quorum, again the NSW legislation provides a model for this
     As for the use of proxies in committee meetings some provision like this is required. Especially for properties that meet frequently, there are times when not all committee members can attend. This can hold up the normal function of a building and stymie progress of important matters
     There has long been a prohibition in other states on purchasers requiring proxies or other powers to be given to the developer and this is an important consumer protection
   - Option 9B – any increase authority to owners corporation managers to make decisions will increase those managers' liability and areas of dispute between an owners corporation and their manager. While this increased authority may be attractive to some managers, PICA believes that a well worded contract of appointment and regular contact with owners means this is not necessary, noting that authorities in emergencies are greater
   - Option 9C – interim resolutions are fraught with difficulties, increased disputed and lack of clarity about when the resolution can be acted on. Rather than the proposed amendment to special resolutions, we would propose that the NSW model be adopted whereby a special resolution is one where no more than 25% *of votes cast* (rather than of all members) are against the resolution. This means the difficulties of low attendance at a meeting are not an issue and the need for interim resolutions is removed

   3.2. Committee size and processes
   - We do not agree that the current maximum size is too large for optimal decision-making. The main size in optimal decision making is having the right people on the committee not the number of people. The maximum of 12 does also allow fair representation of a proportion of owners in larger schemes
   - Option 10A – we do not believe seven is a reasonable number. There are more and more schemes with over 200 lots; they will have significant decisions made by 3.5% of their owner base. We also strongly recommend that a committee be mandatory for all schemes, having to use general meetings for day to day decisions of say a seven lot scheme is not practical when there may be a group of say three owners who are active and willing to form a committee. We do not see the logic in having a limit of seven but allowing the owners corporation to resolve to have up to 12 as per the Options Paper

- Option 10B – we believe that section 111 is clear and that the use of ballots is mainly driven by the need to avoid a physical meeting. The secretary or the owners corporation manager should be permitted to arrange a ballot

4. Dispute resolution and legal proceedings
   4.1. Internal dispute resolution process
   - Option 11A is the most practical solution to this issue. While internal dispute resolution should not be a requirement a mediation option should be available. This would be a low cost alternative to litigation and would likely resolve a number of issues
   - A sub-committee would in most cases be appropriate as utilisation of a professional mediator is likely to be the path to the best outcome for all parties

   4.2. Civil penalties for breaches of owners corporation rules
   - The recently revised penalty regime in NSW, both the amount and who penalties are payable to, is an appropriate model
   - Therefore options 12A and 12C are applicable however, for persons who continually breach rules, more than just $1,100 should apply

   4.3. Initiating legal proceedings
   - Our comments in section 3.1 about a change to how a special resolution is defined would remove the issues with requiring a special resolution. If this is not agreeable, the proposed option 13A is suitable. Options 13B and 13C are not suitable. 13B creates yet another type of resolution and will likely cause even more confusion for members. 13C will also likely lead to confusion, especially if a matter progresses from one court to another

5. Differential regulation of different-sized owners corporations
   - The differing needs of different-sized owners corporations need to be considered along side a need to not over complicate management requirements for both members and owners corporation managers
   - We note the details in option 14A however, we do not believe this is an appropriate breakdown and suggest the following (lots here means occupiable lots – not car or other utility lots):
     - 2 lot schemes – retain their exemptions
     - 3 lots or more – all provisions of the Act apply including the need for an audit and maintenance fund
   - There may be an argument for additional requirements of large schemes (perhaps more than 100 lots) but these may not be necessary

6. Finances, insurance and maintenance
   6.1. Defaulting lot owners
   - Adoption of option 15A is not practical and will not assist in overcoming the problems raised, it will just present another barrier to homeownership
   - Option 15B is a good step, it will be important to have a framework in place about what the obligations of the lot owner (eg what "evidence" of hardship is required, does the unpaid amount continue to incur interest, timeframe for repayment) and owners corporation/owners corporation manager are (eg provision of updates on status of lots under a payment plan to the committee). This should also be able to be managed via committee resolution, not general meeting resolution
   - The issue of costs related to recovery of unpaid fees placing a burden on other owners can be substantially overcome via implementation of options 15C and 15D
   - Options 15E and 15F are also beneficial in making this process more practial

6.2. Insurance

- Option 16A is an essential step in aligning Victorian owners corporations with national best practice. Question 45 about the cost of increasing minimum PL insurance is not appropriate. The minimum will be very different for different properties. The requirement should be that the owners corporation is required to obtain expert advice on this (from an experienced owners corporation broker) and to follow their recommendation as a minimum. Insurance is not an area where a one size fits all approach will work
- Levying the cost of insurance by a different calculation method as per the first dot point on page 52 will require a significant additional accounting burden that is not necessary
- The second dot point on page 52 however has significant merit and should be implemented as should the third
- The fourth dot point needs more caution; the damage may not have been caused by a lot owner (or their guest) and may not have been preventable by the lot owner
- Applying differential levies when lot use increases the risk will be problematic and too subjective. It would be best to have such issues managed by a process whereby, when this happens, the lot owner/s are charged any additional premium and only when this information comes via independent expert eg insurance broker

6.3. Maintenance plans and maintenance funds

- Of the options presented, option 17B is the best however, it is not quite as practical as it may appear
- As per our comments in section 5, all schemes (apart from two lots schemes) should be required to have a maintenance plan. All schemes should also be required to follow it **or** explain why they are not. For example, a plan may call for replacement of a pump but an owners corporation who has been undertaking proper maintenance may be advised by their supplier that replacement is not necessary for another two years – reasonable grounds to not make the replacement when the plan indicates
- Proper use of maintenance funds helps to avoid the need for additional/unexpected levies which can be an significant financial burden on lot owners

6.4. Increased expenditure arising from lot use

- The additional costs for differing lot uses are better managed by setting up a "multi" owners corporation structure where, for example, commercial lots pay their costs and residential pay there costs. It would be better to set up a more formal way for multi owners corporations to work similar to how a building management committee in NSW or building management statement in Queensland is managed

7. Part 5 of the subdivision Act

7.1. Common seals

- The need for a common seal is no longer meaningful, allowing signing by two members of the committee, two members of the owners corporation or the owners corporation manager is sufficient
- The question about risks is worth consideration however, signing with or without a seal is no more or less risky. Seals can just as easily be replicated, most are provided by a stamp company or stationer – signing a document under seal does not provide any more security

7.2. Procedure for initial setting of and changes to lot liability and lot entitlement

- Before considering the method of calculation of lot liability and lot entitlement, the need for two separate sets of numbers is worth considering. The note on page 58 about "equal setting of liability and entitlement where lots are of unequal size" implies that size is the only criteria in setting liability and entitlement which is not correct. A number of

factors should be considered when setting liability and entitlement, size, location, use, etc.
- Of the options presented, 20C is the most appropriate. Recent best practice indicates that market value at a common date is a good criteria (as detailed in section 2.1). With this method there would be no need for separate lot liability and lot entitlement

7.3. Sale and redevelopment of apartment buildings
- Option 21A, the NSW model, is the most appropriate. It is worth noting that this process is still expected to take about two years and significant costs will be involved
- Any model with tiers will make an already complex process unnecessarily complicated

8. Retirement villages with owners corporations
- As PICA does not manage any retirement villages with owners corporations, we do not believe it is appropriate for us to comment on this section in detail
- We do believe that a simpler process is the best across all areas