

SUBMISSION TO CONSUMER PROPERTY LAW REVIEW

Responses to Issues Paper No 1
Part B – Owners Corporation Managers

BY
GREG HONEYMAN
MBCM BALLARAT
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EXTRACT

Owners Corporations are required to be managed. Usually this is by a professional external manager, however some Owners Corporations have the in-house skills to enable them to self-manage. The main purpose of the OC Manager is to protect the best interests of the owners and to assist in ensuring that the value of their investment is maintained and to grow wherever possible. Too many Owners Corporations are simply not set up and are inactive. The cause of this state of affairs is ignorance and apathy on behalf of large sectors of the community, including not just owners, but also many industry stakeholders who should know better (including real estate agents, conveyancers, solicitors, local council planning departments, banks and finance companies, surveyors and architects).

Members of Owners Corporations do not know what they do not know. It is the industry stakeholders' collective responsibility to ensure that they do begin to understand the facts about Owners Corporations, and that they are bound by numerous rules and regulations.

Unfortunately the quality of Owners Corporation management varies enormously, from strata specialist professionals to cottage-industry amateurs (and unfortunately some charlatans). This leads to unacceptable risks as it means that there is a large degree of incompetence in the industry which must be removed as quickly as possible.

In an environment of rapid growth of strata developments and community living, where many millions of consumers' dollars are at stake, it is imperative that management quality is improved so that all owners can have confidence that their Owners Corporation is being managed effectively and both their investment and their combined current fees are protected.

This improvement will only occur if the industry is better regulated and if Managers are licensed. This requirement will lead to numerous other prescriptive and mandated reforms.

AUTHORS' NOTE

This submission is solely the personal view of the author and reflects experiences of the author in the Central Highlands region of Victoria. It is not prepared on behalf of the MBCM Group and does not necessarily reflect the views or either MBCM Head Office management or other MBCM franchisees.

PURPOSE OF THIS REVIEW

- To identify opportunities to improve the professionalism and conduct of Owners Corporation managers.

THIS REVIEW ALSO RAISES ANOTHER QUESTION

- If it is true there is a large variance in the quality and rectitude of Owners Corporation Managers in Victoria, there must be a root cause that has allowed this situation to develop.
- This author believes there is a huge degree of community ignorance in relation to everything to do with Owners Corporations.
- It will be argued as part of this document that for any review of this nature to be successful, it must include efforts to identify the root causes of this ignorance and for government and its agencies together with all industry stakeholders to develop remedial action.

REGISTRATION AND UNSUITABLE MANAGERS

Question 64

Are there benefits in aligning the eligibility requirements for an Owners Corporation manager to the extent practical with those of estate agents?

Yes absolutely. The Owners Corporation management industry has for too long operated as a cottage industry. Whilst this may have been acceptable twenty or thirty years ago, we must realise that this industry now must both function - and be seen to function - as a properly regulated profession. And to be a profession, I have long maintained that Owners Corporation managers must be better regulated, and the bar must continually be raised in relation to quality. Entry to the industry must be made more difficult as it is for real estate agents. This means a licensing scheme must be introduced.

In an environment of considerable ignorance on behalf of many owners (who are too often taken advantage of), the biggest benefit will be to weed out the ineffective, the incompetent and the charlatans, who collectively give our profession a bad name and make life difficult for those of us who do constantly work to build effective relationships with our clients.

Question 65

What are your views on whether Owners Corporation managers should be separately licensed or be part of an estate agent's licence?

Owners Corporation managers are NOT real estate agents. Owners Corporation managers must have their own license with its own regulations. Whilst one argument maintains that licensing schemes restrict entry to the industry, I believe this is totally fallacious. My prior industry experience provides evidence that in fact the more professional an industry is, the more attractive it is to potential entrants, the more it encourages competition and improves mobility of labour. Because our industry is currently almost 'invisible' in that far too many people simply do not know what an Owners Corporation manager or an Owners Corporation portfolio manager does, a licensing scheme would provide opportunities to educate the public about Owners Corporations.

Licensing ultimately would be a positive step to eliminating shoddy, unprofessional and dishonest practices.

Question 66

Is it appropriate to extend the current regulatory criteria to include serious criminal offences?

Yes absolutely. One single incident of serious misconduct (eg theft of owners' funds) creates a disproportionate amount of negative publicity and loss of confidence in the industry. Such a loss of confidence can take years to overcome. It will be considered acceptable to utilise the components of the real estate license that may be appropriate (ie ineligibility to operate or disqualification clauses).

Question 67

What would be the benefits and costs of placing requirements on Owners Corporation managers to hold professional indemnity insurance as a condition of practise?

I cannot believe this question is even being asked. Surely professional indemnity insurance is a fundamental requirement for any professional in any industry to operate. It is certainly a mandated requirement for all franchisees of our MBCM group as well as for membership of the SCA (Vic). For the same reason, the MBCM group will not permit any trades person on any client site (including gardeners) without evidence of current PI insurance.

Anyone who is operating as an Owners Corporation manager without professional indemnity insurance is merely demonstrating a depressing level of incompetence. Any such operators should be removed from the industry.

In relation to 'costs' I would ask what is the cost of not having insurance of this kind.

CONFLICTS OF INTEREST

Question 68

In your experience what is the current practice of Owners Corporation managers in relation to disclosure of commissions?

There seems to be a missing piece of a puzzle in this question. This is the simple fact that Owners Corporation managers do not tell owners what to do. Professional Owners Corporation managers take instruction from owners (just like lawyers). We endeavour to assist members of the Owners Corporation to make informed decisions. In this respect it is incumbent on professional Owners Corporation managers to provide a range of options that are in the best interests of owners. Those managers who fail in this duty should be removed from the industry.

Accordingly, we advise our clients of the best options for any expenditure, whether this is for insurance, gardening, repairs or anything else. It is up to the owners to make the decision of which option to accept. Importantly we do not have any financial association or undisclosed arrangements with any contractors or tradespeople we use to service our client Owners Corporations. This means we do not accept commissions for any work or activity other than for insurance, of which we always advise our owners.

In Victoria, for us as an MBCM franchise and for all Owners Corporation Managers who are members of the peak industry body (SCA Vic), all insurance commissions are absolutely transparent. As an MBCM franchisee, we provide a Disclosure Statement of Commissions¹ in all Management Reports,

¹ Refer Appendix 1: "Disclosure of Insurance Agency Fees and Commissions"

and in fact at every AGM (and whenever body corporate insurance is discussed). Whilst we always obtain a minimum of three quotes from different insurers for every property, in our experience there is no compulsion for owners to accept any of these quotes. There is no impediment to owners who prefer to choose a local insurance supplier – even where this means the insurance policy is not commissionable. We have a number of these insurance policies in place for our owners.

Whilst we embrace disclosure of commissions as an integral part of any meeting, it is the owners who determine where their insurance is placed. Professional managers ensure that Owners Corporations are protected with the best available insurance and insured properly and in a timely manner.

Question 69

Do commissions and discounts have an adverse impact on premiums for insurance, and if so, how does this manifest?

When explained in a factual way, it is accepted by our clients that the payment of insurance commissions to professional managers does not cost unit owners more. Quite the opposite in fact. In our view the current practice keeps costs down. Professional managers undergo training in strata insurance products and are viewed by the insurance industry as a key part of the insurance process, particularly in ensuring that competitive quotations are carried out properly and that owners receive the best possible insurance coverage for their needs at the best possible prices.

Without these professional managers, the insurance companies would have to employ large numbers of sales staff to carry on the job of quoting and providing the correct form of insurance to the many thousands of strata properties in the country. This is what would end up costing the owners more. Not only that, but I have serious doubts whether owners would then end up with the correct insurance. Strata insurance is incredibly specialised. The best people to interface with owners corporations are the professional managers who know the properties and know the owners. The system that is currently in place is the best possible system, and any commissions are well earned, considering the time taken to prepare, organise and deliver quotes.

Generalist and inaccurate comments will result in the worst possible outcome for owners of units in strata communities, both in terms of the quality of insurance and cost. And to expect owners to arrange their own insurance is a recipe for problems, increased cost and potential disaster. The best possible strata insurance is a single blanket cover through one insurer.

- **NOTE: Already commented on is the benefit provided by experienced managers in ensuring the best possible insurance outcome for their clients. A further question in this area is required to explore further the potential impacts where owners attempt to purchase their own insurance. The industry has seen far too many Owners Corporations which have attempted their own insurance and ended up with a disaster on their hands:**
 - Under insurance (and in some cases gross over-insurance).
 - Conjoined units insured by separate insurance companies (ensuring fertile ground for dispute between competing insurance companies in the event of a claim where damage is caused to two or more units).
 - No common property insurance (where owners are ignorant of the requirement, thus exposing them to personal liability in the event of an incident).
 - Expired insurance (MBCM Ballarat is dealing with one of these as we speak, where the owners simply forgot to renew – 15 months ago).
 - Non-existent insurance (of course a disaster won't happen to me).

Question 70

What are the non-regulatory approaches that could be considered to ensure commissions and other payments do not distort the market?

If Owners Corporation managers are honest and have nothing to hide, there is nothing to be feared from disclosing insurance commissions. We personally disagree with earning commissions from trade work, as this leads to possible uncontrolled instances of nepotism, cronyism and conflict of interest.

There are numerous approaches to ensure that commissions do not distort the market, but to make them effective they would probably have to be regulated or mandated. However:

- The industry² must address the ignorance factor relating to Owners Corporations out in consumer land. Through no fault of their own, ignorant people are too easily swayed by impassioned but misguided claims about all manner of Owners Corporation issues, including insurance commissions. Frequently these subjective and contentious arguments are wildly inaccurate. The heat must be taken out of the discussion through plain, clear education. Please refer to this author's accompanying submission which outlines this discussion in much greater detail. The reason people are confused by issues is because they don't understand them.
- Owners Corporation managers should belong to the industry peak body SCA (Vic). They are then bound to uphold industry best practices, including disclosure of commissions.
- Owners Corporation managers should only be permitted to represent an Owners Corporation if they hold a current, standard SCA (Vic) management contract. No other version of management contract should be permitted.
- There should be one single approved disclosure statement across the entire industry (as Appendix 1) for insurance commissions.
- Insurance commissions may not be earned unless the Owners Corporation manager has undertaken suitable industry training (as currently conducted by the major strata insurance companies and undertaken by MBCM franchisees).
- All insurance providers in the strata insurance industry (including brokers) could be more proactive in marketing and promoting the myriad of benefits to owners of utilising professional Owners Corporation managers to assist in ensuring the best possible insurance product is made available for every property.
- In order to prevent the possibility of either perceived or actual secret commissions, Owners Corporation managers should not accept commissions from any tradespeople who work on client property. This fact should be evident in every management contract and in all marketing literature across the entire industry.
- Tradespeople may not be acceptable for work on any Owners Corporation property without demonstration of professional qualifications and current professional indemnity insurance.
- Renegade, dishonest and incompetent Owners Corporation managers must be publicly removed from the industry.
- Improve the quality of positive communications between industry and media outlets. Too often it is the hysterical and pejorative language of a very small minority which creates the biggest media stories, which are invariably negative. This reinforces negative impressions of

² Industry includes all stakeholders: government and its agencies (including Consumer Affairs Victoria) as well as all companies purporting to be OC managers, real estate agencies, local councils, conveyancers, solicitors and any profession involved in the development, marketing, selling and transferring of units in Owners Corporations.

the entire industry, which reflects poorly on the vast majority of professional OC managers who are managing their clients' properties extremely well.

UNFAIR TERMS IN MANAGEMENT CONTRACTS

Question 71

What are the main concerns about unfair contract terms in management contracts?

The main problems occur because owners are greatly confused by contracts and the terms of the contracts (the ignorance factor again). We at MBCM go to great lengths to explain contracts to our clients, and we also produce community education information³ about how to exit management contracts both legally and ethically.

- Managers should not be permitted to manage properties without a valid managers' contract. We have experienced numerous incidences of un-professional managers functioning without any contract. This is extremely dangerous for owners because it leaves them without any protection.
- There must be commonality of management contracts (ie a single prescribed template - refer earlier comment about contracts).
- Committees may not terminate a manager's contract. This can only be achieved by the Owners Corporation.
- Termination of a manager's contract should require a Special General Resolution (ie 75% of owners). As this method offers the opportunity for both owners and manager to prepare a position or rationale, this is the only method that offers the certainty of a reasonable, rational outcome. The vote can be held either by simple majority or by Lot Entitlement.
- No other variations of termination procedure should be considered. The process of termination must be simplified. Ballots are complex, opaque, expensive and time consuming, and are rarely as effective as straightforward voting.
- The supposed issue of not being able to achieve a quorum (because owners may live some distance away or interstate) is fallacious because meetings can legally be conducted electronically, either by telephone, teleconference, Skype or other technology. MBCM Ballarat regularly conducts meetings this way. Having few members attending meetings suits some managers because they find it is quicker and easier dealing with the same group of owners on a regular basis. Managers should make a greater effort to ensure owners attend meetings, and also join committees.
- Such meetings can be held after hours, particularly when the Owners Corporation is prepared to pay the manager a \$2.2 fee for an hour or so of his or her professional time.

Question 72

Are there other types of unfair terms that should be considered? If so, what are they and how common are they? Why might they be unfair?

- Owners can also be completely bamboozled by unethical managers who deliberately fail to notify owners about the approaching end date of their contract, leading to the contract rolling over for a further 12 months.

³ Appendix 2: MBCM Ballarat - "Terminating Your Owners Corporation Manager".

- When the contract term ends, the Owners Corporation should be able to terminate the manager on one month's notice UNLESS a new contract is negotiated and legally signed. This would avoid the issue of automatic roll-over of the contract for a further 12 months and allow frustrated owners to terminate the management contract within a reasonable timeframe.
- It should be incumbent on every manager to remind clients at every AGM of the terms of the contract and also advise when the end date is imminent. This will permit owners to make an informed decision about whether to renew the manager's contract.
- In relation to assignment of portfolios and management contracts, this is relatively straightforward, as owners corporations have the ability to decline the change of manager, regardless of the size of the property portfolio. In our experience, the outgoing manager communicates the fact of the changeover with all owners, and the incoming manager subsequently arranges to meet or speak with owners. The SCA (Vic) approach is good common sense.

ENDING LONG-TERM CONTRACTS

Question 73

Should any distinction be drawn between the required contractual terms for initial and subsequent management contracts? If so, why? How would such a distinction be drawn?

- The maximum allowable term for any management contract should be 3 years. If the manager has performed well, has build strong relationships with owners and has demonstrated capability then they will have no difficulty in confirming a new contract term.

Question 74

What is your view as to contractual terms for the renewal of management contracts? For example, should there be any rules about terms such as automatic renewals or renewals at the prerogative of the manager only?

- It is the manager's responsibility to ensure that he or she has built a strong rapport with owners, wherever they live. All other arguments in favour of automatic roll-overs are merely excuses for lazy or incompetent managers.
- As regards termination of contract, previous comments apply.

Question 75

Are there other issues that require a regulatory response relating to long-term management contracts?

I personally do not believe in long-term management contracts as they are prone to nepotism, favouritism, and conflict of interest

MANAGERS' CONDUCT AROUND VOTING

Question 76

How can concerns about managers' influence on voting be addressed?

The biggest issue here is the fact that committees tend to retain the same members for protracted periods of time. Managers can also work very closely with those committees or owners for lengthy periods, and sometimes this can lead to unfortunate or unhealthy practices.

- The critical factor is to ensure that all owners contribute to decision-making (the ignorance and apathy issue again). This can only be achieved through effective communication and education, and is the responsibility of all stakeholders (see previous comments regarding this).

FINANCIAL TRANSPARENCY

Question 77

How can concerns about fraudulent financial conduct be addressed? Would it be preferable in the context of financial transparency and accountability to require separate Owners Corporation funds to be kept in separate accounts?

MBCM Ballarat maintains separate dedicated accounts for every client. Where a sinking fund exists, this is kept in a further separate interest bearing account. We are passionate about transparency and privacy in everything we do, and separate accounts permit this degree of account dedication.

- Our specialised proprietary management software maintains an accurate financial record of every financial transaction. It is critically important that owners understand the status of their funds and we work hard to ensure that all owners understand that they can request updates of check on the status of payments at any time during working hours.
- For after-hours information, MBCM websites permit every individual owner to log-in to their own Owners Corporation, and to pay fees online, as well as to access their financial status in real time.
- As with MBCM Ballarat, it should be incumbent on every professional manager to provide instant regular financial updates, and certainly on request from any owner or committee as to their financial status (not just once a year at the AGM).

Question 78

What proportion of managers still use pooled accounts, and what would be the realistic costs and time required to transition to the use of separate accounts? Where possible, include the basis for these estimates.

- The vast majority of all MBCM franchisees (currently 47 franchises) introduced separate accounts for all clients in April 2015.
- Clients advise that they appreciate the security and privacy of the new banking arrangements.
- MBCM Ballarat management appreciates the ability to access real time account information and also the ability to automatically reconcile client accounts.
- There was minimal cost for the MBCM organisation as management software is developed in-house.
- I understand there was no cost from Macquarie Bank as they prepared the banking component on behalf of the industry. This should be confirmed with Macquarie Bank.

- MBCM Ballarat charged a fee of \$150 to each client, regardless of size to cover the cost of transferring their funds from the old pooled account and setting up a dedicated account.
- All franchisees were taken through a basic training program to prepare for the changeover.
- The lead-up process from initial communication to final training program took several weeks and was conducted jointly by in-house training with extensive external support by Macquarie Bank.
- Macquarie Bank operates a helpdesk to assist with questions.
- The actual transition process was achieved seamlessly and was completed in one day.

CONCLUSION

As increasing numbers of Victorians own, occupy and work in Owners Corporations, it is heartening to see Government and its agencies working to understand the issues confronting the industry.

If the aim is to protect Victorians and their investments, any changes to legislation as well as marketing such changes must include a concentration on education of all aspects of Owners Corporations. This must naturally include existing owners and purchasers, but must also consider vendors, and every profession connected to the development, planning, approval, construction, marketing, selling, financing and transacting of strata community real estate.

As heartening as it is to have an opportunity to participate in the research phase of amending legislation, until all stakeholders across the spectrum of Owners Corporations understand Owners Corporation legislation as well as their own responsibilities, the problematic issues around Owners Corporations will continue to multiply and property owners will continue to be aggrieved.

ABOUT MBCM BALLARAT

MBCM Ballarat is known for providing professional and reliable strata management solutions in our clients' local communities. Specialising in the set-up and professional management of residential, commercial and industrial Owners Corporations, we are committed to providing our clients with industry leading service and expertise.

MBCM is the only brand in Strata Management that thinks globally and acts locally. The marriage between the best systems and imparting these at a local community level, through motivated and passionate franchise owners, is truly unique. It's this unique quality that ensures we develop and maintain strong relationships with each of our Owners Corporations and the reason for our enduring success since 1987.

MBCM Mission

We act on behalf of local strata corporations to ensure their common property is well-maintained and protected. To this end, we guide the decision making process and we manage common property projects so as to improve the value of our clients' properties.

MBCM Vision

To be recognised as Australia's leading strata management brand operating at a local community level through motivated and passionate franchisees.

APPENDIX 1

Every MBCM Ballarat Manager's Report and insurance document delivered at Annual General Meetings carries the following disclosure:

SCA (Vic) DISCLOSURE OF INSURANCE AGENCY FEES AND COMMISSIONS

The purpose of this memorandum is to facilitate uniform disclosure of insurance agency fees and commissions received by Owners Corporation Managers who are members of Strata Community Australia Victoria and who comply with the conditions set out below.

Strata Community Australia endorses the current practice of Managers deriving insurance commissions on insurance premiums paid on behalf of Owners Corporations as this contributes to a lower level of management fees and has no effect on the cost of insurance to the Owners Corporation.

The conditions applicable to endorsement by the Institute are as follows:

1. Such fees and commissions are properly disclosed to clients.
2. Such fees and commissions do not increase the cost of insurance to Owners Corporations.
3. Such fees and commissions do not exceed 20% of total premium payable by Owners Corporations.
4. In all cases the best interest of the client is the paramount criterion when presenting quotations from particular insurance companies or placing insurance with any insurance company or broker.

The level of insurance agency fees or commissions by Owners Corporation Managers varies and it rarely reaches the limit set in condition 3 above. This upper limit of such income has been specified in this memorandum to simplify the process of disclosure.

The distribution of this document by the Manager to the Owners Corporation clients will serve as an announcement that such income is being received and that there is compliance with the restrictions as set out above.



STRATA TALK

STRAIGHT TALK ABOUT OWNERS CORPORATIONS

No 18. Terminating Your Owners Corporation Manager

HOW TO PART COMPANY WITH YOUR OWNERS CORPORATION MANAGER

So you are unhappy with your Owners Corporation manager. Your OC has decided to part company with your current manager, but how do you go about terminating your OC manager's contract - legally and ethically?

From our experience, this is one of the most commonly asked questions that we deal with. Here at MBCM we provide you some insights into the legal requirements and timeline that you can work with to achieve a satisfactory outcome for your Owners Corporation.

The first thing you need to know is that your current manager's Contract of Appointment is in fact a legal contract – it will specify that you need to give at least 28 days' notice of your intention to terminate the contract. The minimum notice of 28 days must be before the expiry date of the contract. This contract is a legally binding document between the two parties and cannot be terminated before the expiry date unless mutually agreed by both parties. All contracts will outline conditions of termination.

If you fail to give notice to terminate the Contract of Appointment in sufficient time, the Contract of Appointment will automatically roll over for a further 12 months at the expiry date.

Who makes the decision?

The decision to terminate your manager's Contract of Appointment is a decision of the Owners Corporation and not a decision of an individual member or committee. Usually the committee decide that a change of management is required - the chairperson and/or secretary can then convene a Special General Meeting (SGM), and issue a notice to all members of the Owners Corporation outlining the motion to terminate the current Contract of Appointment with the current manager.

The Owners Corporation by ordinary resolution can terminate the Contract of Appointment. An ordinary resolution requires at least 50% of all lot entitlements voting in favour. Most Contracts of Appointment coincide with the date of the AGM, so action is required

well before attendance at the Annual General Meeting (AGM). Action can be via an SGM or postal ballot.

It is important to recognise that most AGM's and SGM's held by Owners Corporations fail to achieve a quorum (50% of owners) either physically attending or by giving their proxy. Therefore, any decision made to terminate the current manager will only be an interim decision and a period of 28 days must pass with not less than 25% of owners objecting to the decision for the decision to become final.

Notices of an AGM or SGM must be sent to all owners at least 14 days prior to the meeting date. An AGM or SGM may be called by the Owners Corporation Chairperson or Secretary. An SGM may also be called by any lot owner whose lot entitlements total at least 25% of all lot entitlements.

The importance of Timing

Not allowing sufficient time to take all the necessary legal steps could mean you are locked in with a manager you are unhappy with for a further 12 months.

What happens next?

If there is a valid contract, the manager may need to be paid out for the remainder of the contract. The existing OC manager will be required to return all records and funds to the new manager or secretary within 28 days of termination of appointment.

What if you get it wrong?

Proper procedures must be followed. If pursuant to section 119(6) of the Act, the contract has been terminated by the Owners Corporation prior to the end of the term, the manager can claim damages.

As a general rule the manager would only be entitled to make a claim for loss of profits, not the full annual fees. As a rule of thumb, profit costs would generally be approximately 20% - 25% of the annual fees, but, if disputed, evidence and records justifying the loss of profits would have to be produced.

For further information, visit

Website: www.mbcmballarat.com.au

Email: info@mbcmballarat.com.au

Phone: Greg Honeyman: 0434 566 127

