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Investors caught flat-footed when flat needs fixing

Michael Pollak

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Professionals need insurance for those unexpected health problems and so does your building, writes Michael Pollak.

With rental properties in short supply in major cities, apartment investors can make good money - provided they do their homework and are prepared for the occasional pitfall such as urgent, costly repairs.

There is also the problem of dealing with an owner's corporation (made up of all the owners in the strata scheme), making it advisable for investors to do their initial homework, then to attend quarterly meetings of the body corporate and (most importantly) to be at the annual general meeting. A poorly performing corporation can make life difficult indeed.

However, the major problem remains paying for maintenance shocks - older buildings are particularly vulnerable to such shocks. Such problems can be made even worse, strata managers warn, if the quarterly levies do not raise enough money and if the sinking fund starts to sink.

Concrete cancer is one of the more devastating problems of building maintenance, according to Chris Parker, director of Sydney-based Michael Roberts Strata Management. He says repairing concrete can cost more than \$300,000, to be raised over 18 months. This can include such added work as balconies being removed and fixed.

Parker believes surprises like this shouldn't happen in a properly maintained building. He says well-run stratas will always have enough money in the sinking fund, and he urges investors to ensure this is so.

A well-run building should also present well. "An investor should always keep an eye on the appearance of the lobby, pathways and garden, and there should be alarm if there is evidence of neglect or disrepair," he says. "If an investor sees shoddiness anywhere the question has to be asked: why aren't these things being attended to?"

Other maintenance issues include the cost of lift upkeep and improvement, which can be about \$35,000 a year.

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In Queensland, one of the hidden, and increasing, maintenance problems over the past five years involves termites, which are causing treatment upgrades often costing up to \$47,000. This was the case at a gated community of 70 townhouses in south-east Queensland where owners had to raise this amount in a special levy, collected over four quarterly payments. Other funds had to be found for the resurfacing of the main roadway within the common property.

As well as noting those maintenance items, Josephine D'Arcy, principal of Brisbane-based strata manager Capitol Body Corporate Administration, also tells of up to \$60,000 being regularly needed to repair corroded windows in older buildings.

D'Arcy says investors should be aware of how much is in the sinking fund "and if this amount is insufficient it must be assumed that extra costs will be incurred", adding that it's preferable to pay more in quarterly levies than not enough. "We try to set levies at above the inflation rate to be ready for any emergencies," she says.

Every investor is advised to keep a finger on the pulse of every facet of the owners' corporation. "It's important to participate, to have knowledge," she says.

Although D'Arcy, like Parker, always tries to avoid special levies, she thinks it's a good idea for investors to keep a grubstake at the ready for such a contingency.

Parker urges prospective buyers to not only search all relevant documents, such as the minutes of strata meetings, but also to door-knock throughout the building to learn as much as they can.

Cosmetic improvements are one thing but funds for emergency repairs (in some cases demanded by government authorities) often have to be found quickly. If the sinking fund can't provide it and there is resistance to a special levy, an alternative arrangement is the new concept of strata financing, so far provided by only three companies throughout Australia.

Strata financing is a contentious issue, with stringent conditions. In NSW, it requires a special annual general meeting resolution and in effect needs 75 per cent approval; in Queensland it requires a unanimous resolution. One of the pioneers of this mechanism is Sydney-based Strata Finance, whose managing director, Bill Debney, regards it as "a true user-pays approach".

"The owners' corporation can negotiate more-competitive building contracts, secure in the knowledge you have the funds, rather than awaiting owners to pay lump-sum special levies," Debney says.

Strata Finance, which has operated for four years, treats each loan application on its merits, depending on the type of property, the state of its finances and the level of risk involved. Debney

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describes one typical arrangement as a loan at a fixed rate of 10.5 per cent over a term of three to five years. The amounts lent have ranged from \$50,000 to "many millions".

"In four years we haven't had a default as a result of our initial credit analysis of each owners' corporation," says Debney, who notes that his loans require no personal guarantees, liens or mortgages for owners, whose credit rating would not be affected.

Strata managers have not yet warmed to strata financing, one describing it as "a relatively new thing, and people are uncomfortable with it", and another as "something I wouldn't recommend at this time".

Debney sees it as an important tool to provide funding for urgent maintenance work, without which "too many properties will slide into becoming the slums of tomorrow".

If, at an AGM near you, there is talk of repairs or grandiose plans for beautification, you'd better be there to follow the money trail.

On the mend

- Apartment investors must be prepared to pay for maintenance.
- There should always be enough money in the strata sinking fund.
- If there is not enough in the sinking fund, special levies or strata finance can be used.

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