

## **REFORM OF STRATA SCHEME LAWS IN NSW**

Legal Aid NSW Submission

to

NSW Fair Trading

August 2015

### About Legal Aid NSW

The Legal Aid Commission of New South Wales (Legal Aid NSW) is an independent statutory body established under the *Legal Aid Commission Act 1979* (NSW) to provide legal assistance, with a particular focus on the needs of people who are economically or socially disadvantaged members of society.

We are the largest legal aid agency in Australia, playing a central role in the delivery and coordination of legal aid services, with a state-wide network of 21 offices and 194 regular outreach locations.

Legal Aid NSW provides information, community legal education, advice, minor assistance and representation, through a large in-house legal practice and private practitioners. Legal Aid NSW also funds a number of services provided by non-government organisations, including 35 community legal centres and 28 Women's Domestic Violence Court Advocacy Services.

The Legal Aid NSW Civil Law Division focuses on legal problems that impact most on disadvantaged communities, such as tenancy and housing, debt, employment, social security and access to essential social services.

Legal Aid NSW civil law solicitors advise and represent clients living in social and public housing, as well as home owners, with a particular focus on clients experiencing, or at risk of, eviction or homelessness. This submission draws on the casework experience of civil law solicitors in providing these services.

Legal Aid NSW has made several submissions relating to legal and policy issues impacting on housing and financial hardship, particularly in relation to disadvantaged groups, including:

- the NSW Family and Community Services Inquiry into Social Housing<sup>1</sup>
- the Legislative Council Inquiry into Social, Public and Affordable Housing,<sup>2</sup>
- the Legislative Assembly Committee on Legal Affairs Inquiry into debt recovery in NSW<sup>3</sup>
- the Public Accounts Committee Inquiry into Tenancy Management in Public Housing, and<sup>4</sup>
- The Productivity Commission Access to Justice Arrangements Issues Paper.<sup>5</sup>

### **Casework experience in strata matters**

Legal Aid NSW commonly advises people seeking assistance in relation to strata disputes in a Court or Tribunal, and in some circumstances will also provide legal representation. People seeking legal advice from Legal Aid NSW about strata issues generally present with a problem that falls into one or more of these categories:

- Unpaid levies and related expenses
- Neighbourhood type disputes
- Disputes between owners and owners corporations about repairs and maintenance, and
- Complaints about the management of the strata scheme.

Since 2001 Legal Aid NSW has provided over 2,500 advice services in relation to strata disputes. One fifth (20%) arose from complaints about the management of strata scheme. Almost one third (28%) of these matters related to unpaid levies. Solicitors regularly provide further assistance to clients with these problems by negotiating on the client's behalf to resolve matters prior to judgment.

Legal Aid NSW welcomes the opportunity to respond to the Draft *Strata Schemes Management Bill 2015* and Draft *Strata Schemes Development Bill 2015*.

Should you require further information or would like to discuss any of our recommendations, the contact officer is Rebekah Doran, Senior Solicitor Consumer Law.

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<sup>1</sup> [http://www.legalaid.nsw.gov.au/\\_\\_data/assets/pdf\\_file/0003/21792/Legal-Aid-NSW-submission-to-FACS-Social-Housing-in-NSW-Discussion-Paper-Feb-15.pdf](http://www.legalaid.nsw.gov.au/__data/assets/pdf_file/0003/21792/Legal-Aid-NSW-submission-to-FACS-Social-Housing-in-NSW-Discussion-Paper-Feb-15.pdf)

<sup>2</sup> [http://www.legalaid.nsw.gov.au/\\_\\_data/assets/pdf\\_file/0010/18955/ASIC-Consultation-Paper198-database-for-small-amount-lenders-2.pdf](http://www.legalaid.nsw.gov.au/__data/assets/pdf_file/0010/18955/ASIC-Consultation-Paper198-database-for-small-amount-lenders-2.pdf)

<sup>3</sup> [http://www.legalaid.nsw.gov.au/\\_\\_data/assets/pdf\\_file/0007/19582/Legal-Aid-NSW-Submission-Inquiry-into-debt-recovery-in-NSW.pdf](http://www.legalaid.nsw.gov.au/__data/assets/pdf_file/0007/19582/Legal-Aid-NSW-Submission-Inquiry-into-debt-recovery-in-NSW.pdf)

<sup>4</sup> [http://www.legalaid.nsw.gov.au/\\_\\_data/assets/pdf\\_file/0006/19959/Legal-Aid-NSW-submission-Inquiry-into-Tenancy-Management-in-Social-Housing.pdf](http://www.legalaid.nsw.gov.au/__data/assets/pdf_file/0006/19959/Legal-Aid-NSW-submission-Inquiry-into-Tenancy-Management-in-Social-Housing.pdf)

<sup>5</sup> <http://intranet/Practice/LawReform/Pages/LawReform-General.aspx>, February 2014.

## Summary of Submission

Legal Aid NSW supports the proposed expanded jurisdiction of the NSW Civil and Administrative Tribunal (“NCAT) to deal with strata disputes. This will provide a much needed, low cost decision making forum for the full range of disputes that can arise between owners, owners corporations and strata managers with limited need for legal representation. We also support the continuation of the strata mediation service and the proposed free advocacy program and advice service for owners.

However, Legal Aid NSW has identified a number of areas where the process could be improved in order to meet the objectives of the proposed reform. In particular, the internal dispute resolution processes could be improved to develop efficient, non-legal processes for the early resolution of disputes consistent with the direction of the NSW Civil Justice Strategy being developed by the Department of Justice.

Legal Aid NSW is also concerned about the following specific areas of the proposed strata scheme reforms:

1. Unpaid levies:
  - a. The absence of a statutory right for owner occupiers experiencing financial hardship to seek a variation of their payment obligations
  - b. Inadequate arrangements for an owner whose unit is uninhabitable due to an act or omission of the owners corporation
  - c. Insufficient notice requirements for owners in default, and
  - d. The absence of any regulatory limit on enforcement expenses.
2. Neighbour disputes: the use of civil penalties as a means of enforcing by-laws
3. Dispute resolution: the absence of mandatory internal dispute resolution, and
4. Termination of an existing strata scheme: inadequate protections for vulnerable home owners where a decision is made to liquidate the scheme.

These concerns are elaborated further below as follows:

[Part A - Strata Schemes Management Bill 2015 – Unpaid Levies](#)

[Part B - Strata Schemes Management Bill 2015 – Neighbour Disputes](#)

[Part C - Strata Schemes Management Bill 2015– Dispute Resolution](#)

[Part D – Strata Schemes Management Bill 2015 – Other matters](#)

[Part E – Strata Schemes Development Bill 2015 – Termination of Schemes](#)

[Part F – Recommendations](#)

## Part A – Strata Schemes Management Bill 2015 – Unpaid Levies

### 1. Non-payment of levies due to financial hardship

Legal Aid NSW is concerned that the draft Strata Schemes Management Bill (“SSMB 2015”) does not provide adequate processes for an owners’ corporation to work with owner occupiers who cannot pay their levies on time due to financial hardship.

#### *The nature of financial hardship – experience of the Mortgage Hardship Service*

Legal Aid NSW often assists clients who are experiencing financial hardship and unable to meet their day to day financial obligations. Financial hardship may be short term or long term and is usually caused by a sudden or unexpected change in circumstances. For those on low incomes, unexpected expenses, such as medical bills or special levies, can also give rise to financial hardship.

The Law and Justice Foundation of NSW (JLF) in its review of the Mortgage Hardship Service<sup>6</sup> identified the following reasons for financial hardship for home owners using the service, which may often exist concurrently.

40.6%	unemployment or reduced employment
28.6%	illness or injury
28.6 %	business failure or reduced income from self-employment
17.7%	family breakdown

These circumstances are often cited as the main reasons for clients being unable to pay bills such as loan repayments, rent, council rates, strata levies, insurance premiums and other consumer contracts.

Using the hardship rights afforded by the credit law,<sup>7</sup> the Mortgage Hardship Service solicitors were able to assist home owners in financial hardship to retain their home or, where this was not possible, sell with dignity with minimum enforcement and other costs. Of the clients assisted by Legal Aid NSW through its Mortgage Hardship services:

- 56.5% were able to retain their home with a hardship variation to get them back on track
- 11.3% sold their house on a timetable agreed between the parties using a hardship variation
- 11.3% surrendered their property to the mortgagee, and
- 17.7% had outcomes that were pending or not unknown at the time of the report.

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<sup>6</sup> Suzie Forell and Michael Cain, ‘Managing Mortgage stress: evaluation of the Legal Aid NSW and Consumer Credit Legal Centre Mortgage Hardship Service’ (2011) *Law and Justice Foundation of NSW* at 38.

<sup>7</sup> s.72 National Credit Code (Schedule 1 of the *National Consumer Credit Protection Act* 2009), previously Uniform Consumer Credit Code

The use of hardship variations as provided under consumer credit regulations provided a way in which credit providers and people in financial hardship could agree on a timeframe to sell, surrender or get back on track with loan repayments. Importantly, it enabled many borrowers to retain their home, with numerous ongoing benefits to the individual and society.

In the years since the LJF study, hardship processes have become imbedded in the business models and practices of all major lenders, and Industry Codes of Practice for banks<sup>8</sup> and non-bank lenders<sup>9</sup>.

The experience of using hardship variations in relation to the provision of regulated credit provides insight into how hardship arrangements may be used to deal with unpaid strata levies where there is financial hardship. Although there are differences between levies owing to an owners corporation and loan repayments, the consequences for owners are the same – namely the loss of one's home. It is therefore critical to have appropriate processes that balance the interests of the owner with that of the owners corporation.

*Response to the proposed hardship provisions in section 85 of the SSMB 2015*

Legal Aid NSW submits that the proposed section 85(4) SSMB 2015, which empowers an owners' corporation to enter a payment plan by resolution, is inadequate for the following reasons. As currently drafted, the entry of parties to a payment plan:

- is voluntary
- can only be made by resolution
- is not dependant on any particular ground
- does not provide options to waive or reduce penalty interest or other charges, and
- specifically allows the continuation of enforcement action to recover the amount while the payment plan is in place.

These proposed provision is not likely to address the problem of owners corporations, and more commonly managing agents, who have been delegated levies collection functions and rarely agree to payment plans, and who instead pursue enforcement of unpaid levies regardless of the circumstances of the owner. An example of this is outlined in Case Example 1 on page 6 of this Submission.

Legal Aid NSW is further concerned that specifying a payment plan must be determined by a resolution of the owners corporation, may inadvertently provide a further impediment to establishing payment plans because:

- meetings are often difficult to arrange
- other matters relating to the collection of levies are usually delegated to a managing agent
- holding a meeting with the assistance of a managing agent incurs additional costs for the owners corporation, and

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<sup>8</sup> ABA Code of Banking Practice, latest version 2013

<sup>9</sup> Mortgage and Finance Association of Australia Code of Practice, latest version April 2014 2014

- without the existence of substantive rights requiring the owners corporation to reasonably consider the proposal, an owner is unlikely to be willing to reveal the details of their financial difficulties to their neighbours.

***Case Example 1: seeking a payment plan for unpaid levies***

The client was a survivor of domestic violence living in a strata unit owned jointly with her partner. On the client's behalf the legal service was successful in obtaining:

- a) an Apprehended Domestic Violence Order excluding the violent partner from the home;
- b) a hearing date in the Family Court to resolve her property dispute;
- c) a hardship variation with the first registered mortgagee, allowing time for the Family Court proceedings to resolve and likely order the sale of the home; and
- d) hardship variations or payment plans with other credit and service providers.

Despite the client having a hearing date set and all other arrangements in place, the owners corporation refused to negotiate any payment arrangement and instead obtained judgment against the client for unpaid levies, interest and enforcement costs in the Local Court.

The owners corporation's solicitor indicated their intention to proceed to bankrupt the client. However, the legal service succeeded in obtaining an order to pay instalments of \$20 per week. Given the disadvantaged position of the client, it is likely that she would be been made bankrupt by the owners corporation had she not been legally represented.

The above case example is particularly concerning because bankruptcy would have had the effect of exacerbating the disadvantage and vulnerability of this woman, particularly in the context of her escaping domestic violence.

Legal Aid NSW submits that a clearly set out, mandatory hardship process is the preferred way to ensure that proposals for a payment arrangement are properly considered. This approach is consistent with the direction of the proposed NSW Civil Justice Strategy which promotes early, cost effective and user-centred responses to resolving legal problems. It also supports the comprehensive hardship provisions available at the Commonwealth level assisting home owners to reach arrangements with their mortgagees.

*An alternative way to deal with unpaid rates*

To address the problems set out above, Legal Aid NSW submits that the SSMB 2015 should establish a statutory right to seek a hardship arrangement for owner occupiers experiencing financial hardship due to illness, unemployment, family breakdown, or other reasonable cause. This would:

- establish a clear process for payment arrangements where there are circumstances of financial hardship
- provide owners with an opportunity to recover from temporary hardship and retain their home or, if this is not possible, sell their property, and

- bring strata schemes regulation in line with best practice in consumer credit,<sup>10</sup> general insurance,<sup>11</sup> energy<sup>12</sup> and telecommunications,<sup>13</sup> where consumers are given protections when in financial hardship.

Legal Aid NSW also supports establishing simpler processes for the payment of special levies by instalments. Although the burden of special levies is likely to be eased over time with the requirement to establish a 10 year capital works plan, special levies can still be challenging, particularly for low income owners. Legal Aid NSW suggests establishing a Non Interest Loan Scheme<sup>14</sup> for owners on low incomes and/or Centrelink benefits to assist with payment of special levies.

To be effective, such a process would need to go hand in hand with a default notice advising the owner of their rights in circumstances where they are experiencing hardship, a cap on the cost of enforcing unpaid levies and an effective internal dispute resolution process as discussed below.

## Recommendations

1. The strata scheme provide statutory protection where owner occupiers are unable to meet their obligations temporarily due to unemployment, illness, family breakdown or other reasonable cause. Options should include one or any combination of:
  - postponing the due date of a payment or payments
  - reducing the amount required to be paid for a period of time
  - a payment plan to catch up on unpaid or postponed levies
  - waiving or reducing penalty interest and enforcement expenses, or
  - any other arrangement that will enable the owner to meet their levies obligations in the future.
2. The regulations establish a process for dealing with hardship applications, including an internal dispute resolution mechanism.
3. While a request for a variation is pending or approved, penalty interest should not accrue on the unpaid levies and debt collection activity should remain on hold.
4. Applications under hardship provisions if rejected can be referred to NCAT for a determination.
5. The cost of dealing with hardship applications is not to be considered as an enforcement expense under section 86 of the SSMB 2015.

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<sup>10</sup> National Credit Code (Schedule 1 of the *National Consumer Credit Protection Act 2009*),

<sup>11</sup> *General Insurance Code of Practice 2014* (Cth)

<sup>12</sup> All energy retailers must have a hardship policy approved by the Australian Energy Regulator:  
[http://www.aer.gov.au/retail-markets/energy-retailers-customer-hardship-policies#Retailers\\_customer\\_hardship\\_policies](http://www.aer.gov.au/retail-markets/energy-retailers-customer-hardship-policies#Retailers_customer_hardship_policies)

<sup>13</sup> *Telecommunications Act 1997* (Cth) Schedule 3 (“Telecommunications Code of Practice 1997”)

<sup>14</sup> See for example the Good Shepard Micro Finance No interest Loans Scheme:  
<http://goodshepherdmicrofinance.org.au/services/no-interest-loan-scheme-nils>

6. In relation to special levies:

- the hardship process also apply to the imposition of special levies, where the payment of those levies would cause substantial hardship, and
- OFT consider establishing a no interest loan scheme to assist low income owners to meet the cost of special levies in a timely way.

## 2. Payment of levies while a unit is uninhabitable due to an act or omission of the Owners Corporation

Legal Aid NSW is aware of people who do not to pay levies due to disputes about repairs to the unit or common property, which are the responsibility of the owners corporation. An example of this is outlined in Case Example 2 below. While these types of disputes are likely to be less protracted with the expanded jurisdiction of the NCAT, Legal Aid NSW proposes that specific provisions be inserted in the SSMB 2015 to address circumstances where a unit is uninhabitable due to an act or omission of the owners corporation.

### **Case Example 2: Rental expenses due to an uninhabitable strata unit**

Our client is an aged pensioner who had lived in his unit since 1984. He has no assets beyond his unit and his only income is Centrelink income. In late 2011 he became very ill and was admitted to hospital and was subsequently discharged into the care of a nursing home type hostel because he had not sufficiently recovered to care for himself independently. By mid-2012 he was sufficiently mobile to care for himself and intended at that time to move back into his home.

On attending his home, he discovered that there had been such a deterioration of the condition of the unit that it was uninhabitable. This deterioration was caused by the failure of the owners corporation to carry out repairs for an extended period, despite his regular requests that they do so. Failure to carry out repairs allowed the ingress of water.

As the unit was uninhabitable he had to remain in the hostel paying an amount of \$570 a fortnight initially, rising to \$620 per fortnight. He has had to pay this rent since mid-2012. Due to the requirement to pay rent he was unable to keep paying the levies on his unit and therefore fell behind. He was also unable to pay the rates as and when they fell due.

Eventually the client successfully advocated for the repair of the unit. This lobbying resulted in the first and most significant aspect of the repairs being undertaken and which allowed him to move back into the unit in mid-2014. There was no dispute that the repairs were the responsibility of the owners corporation, although the issue as to whether the unit was uninhabitable because of the failure to carry out the repairs in a timely way was more controversial.

In early 2014 solicitors for the owners corporation commenced proceedings in the Local Court seeking approximately \$4,000 in unpaid levies. The client did not have money available to pay the debt. The only reason he fell behind in making these payments is that he was required to live elsewhere as a result of the unit being uninhabitable. The solicitor for the owners corporation indicated that it was usual practice to pursue bankruptcy once the debt reached the bankruptcy threshold.

The Legal Aid NSW negotiated for the payment of the entire amount in one lump sum and the withdrawal of the Statement of Claim (and the avoidance of further legal costs). Further information about enforcement costs in this matter is featured in Case Example 4 below.

## Recommendations

7. Amendments be made to the SSMB 2015 to establish a process to assist owners if they must rent elsewhere due the unit being uninhabitable as a result of an act or omission of the owners corporation. Options include:
  - Specifying that owners may seek orders in the NCAT for compensation for loss suffered in these circumstances
  - Requiring an owners corporation to claim on their building insurance to cover the cost of the owner's rental accommodation
  - Suspending the requirement for the owner to pay levies for the period in which the unit is uninhabitable, or
  - Entering into hardship arrangements enabling levies to be paid during the period in which the unit is uninhabitable.
8. Explore options for specific measures to provide compensation for an owner whose property is uninhabitable as a result of an act or omission of the owners corporation.

### 3. Notifying owners about unpaid arrears

Legal Aid NSW assists people in circumstances where they have not been provided with sufficient notice about the commencement of legal proceedings. Appropriate notice is critical for owners to enable them to rectify the default where possible and avoid legal proceedings commencing.

## Recommendations

9. Section 86 of the SSMB 2015 be amended to require an owners corporation to issue a notice in writing before commencing legal proceeding with the following information:
  - the total amount due
  - the components of this amount – levies, interest and enforcement costs
  - a statement that legal proceedings will commence if the amount is not paid within 30 days
  - a statement of any new amounts that will also become due within the 30 days, and
  - a statement that if the person is experiencing financial hardship they may seek assistance from the Financial Counselling Hotline by phoning 1800 007 007.
10. The form of this notice be prescribed in the Regulations.
11. If our recommendations in Section 1 of Part A above are adopted, information is provided about how to make a hardship application.

#### 4. Cost and process of collecting unpaid levies

Legal Aid NSW assists people who have a debt to their owners corporation as well as a related debt for 'enforcement expenses' incurred by the managing agent and/or their solicitors in attempting to recover the amount. Currently, both amounts are treated as a debt to the Owners Corporation under section 80 *Strata Scheme Management Act 1996*.

The principal debt for unpaid levies owing to the owners corporation are typically for modest amounts that are less than the threshold for a bankruptcy application (currently \$5,500). 'Enforcement expenses' added to the unpaid levies are regularly for amounts equivalent to the principal debt, and these two debts combined often take the client over the threshold for bankruptcy which, if pursued, could entrench an owner further in financial difficulties that significantly impact on their life.

##### *Regulation of enforcement expenses*

Legal Aid NSW notes that the current legislation is geared toward litigation as the first response to unpaid levies. The system builds financial incentives for Managing Agents, who often have delegated power to deal with all matter relating to the collection of levies, and the solicitors they instruct, to opt for expensive litigious processes over negotiation and alternative dispute resolution.

This continues to present a problem in the SSMB 2015 because there are no provisions that:

- require enforcement expenses be set at a reasonable level
- provide fee scales establishing a limit on what can be charged for certain items<sup>15</sup>
- encourage widely accepted industry codes or guidelines outlining best practice,<sup>16</sup> and
- provide any external oversight of the expenses incurred, other than of amounts claimed in court proceedings.<sup>17</sup>

Unpaid levies cases are the second largest group of disputes in the Local Court after unpaid council rates.<sup>18</sup> Case examples 3 and 4 below are emblematic of this. This situation is at odds with legislation and codes of practices in almost all other areas of the civil justice system which establish processes and price signals that encourage the use of early, low cost, non-court means of resolving disputes.<sup>19</sup>

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<sup>15</sup> Such as is provided for by s.59 *Legal Profession Uniform Law Application 2014*

<sup>16</sup> Such as *Debt Collection Guideline: for collectors and creditors* (Cth), The Australian Competition and Consumer Commission (ACCC) and the Australian Securities and Investments Commission (ASIC), 2015.

<sup>17</sup> *Owners of Strata Plan 36131 v Dimitriou* [2009] NSWCA 27

<sup>18</sup> Historically reported in The National Alternative Dispute Resolution Advisory Council, *ADR Blueprint*, Research Discussion Paper No 321321 (2009). We understand that this continues to be the Local Court experience.

<sup>19</sup> The objective of the *Civil Procedure Act 2005* (Cth) is to achieve the just, quick and cheap resolution of dispute (s.56). Also see example in the credit space where, if a borrower is in default on a credit contract, financial service providers must serve a default notice with details of their internal dispute resolution process and the external dispute resolution scheme to which they are a member. The EDR schemes then charge FSPs more the longer it takes a dispute to resolve: [www.fos.org.au](http://www.fos.org.au)

**Case Example 3: Unpaid levies and enforcement expenses**

The client is on a Centrelink Pension and had been renting out his strata unit for a number of years and never missed a payment. Levies notices during this time were sent to his alternative address. When the client moved into the unit, he did not receive levies notices for a period of 6 months, by which time he contacted the managing agent to enquire about his levies. No phone calls had been made during this time to enquire why he had not paid levies or whether he had received the notices posted to his old address.

The managing agent then sent the client a notice for the levies plus interest for the late payments. The client was willing to pay the unpaid levies by instalments, but disputed the interest fees due to the circumstances.

The client requested mediation but the owners corporation instead filed proceedings in the Local Court. The total claimed was a modest sum of \$1,700, about half of which consisted of interest and enforcement costs.

**Case Example 4: inappropriate use of bankruptcy proceedings**

The client has owned her strata unit for approximately 10 years. The unit was purchased using a workers compensation payout after suffering serious injury on the job. Since the injury the client has struggled to maintain employment. She is in receipt of the Newstart Allowance and has no other assets.

The client attempted to negotiate an arrangement with the solicitor for the owners corporation and advised that the unit was purchased with the proceeds of workers compensation payments. The solicitor advised that they would proceed to bankrupt the client. This is despite the unit being a protected asset by virtue of being purchased by workers compensation payments.

The original statement of claim sought just under \$7,857 in unpaid levies, costs and interest. The matter was listed in the Full Federal Court 12 months later for a sequestration order seeking a total of \$18,000, consisting of:

\$10,440	–	unpaid strata levies
\$156.73	–	post judgement interest
\$1,669.41	–	debt recovery expenses
\$5,926.60	–	lawyer's fees

The client was fortunately able to borrow money from a friend to cover the levies component of the debt and is placing the property on the market. To complicate matters, the client's unit has been damaged by builders hired by the owners corporation. The dispute remains unresolved at the time of writing.

*Effect of the decision in The Owners of Strata Plan 36131 v Dimitriou (2009) NSWCA 27*  
("Dimitriou")

*Dimitriou* is a significant decision of the Court of Appeal that protects people living in strata arrangements in NSW. *Dimitrou* currently offers some protection for owners in finding that section 80 enforcement expenses must be:

- first, reasonably incurred and reasonable in quantum, and
- second, claimed in the same proceedings as the debt to which they relate.

The effect the first finding is to allow for external scrutiny of enforcement costs in the absence of any other oversight or protections. However, this finding has had limited impact in practice because owners are usually unwilling to contest the reasonableness of enforcement expenses, given the risk of incurring further enforcement expenses in the process.

In relation to the second finding, the Court stated at paragraph 102:

The Owners Corporation was entitled to recover legal costs incurred in the Local Court proceedings, but only to the extent that the rules permitted the recovery of such costs. That was because the mere entitlement to recover "expenses" did not carry with it a right to recover all legal costs properly and reasonably incurred in circumstances where the court in which the proceedings were brought could not or did not permit recovery of all such costs. To permit additional recovery would be to set at nought the terms of the Civil Claims Act or, in relation to other courts, the order of the court which was not the subject of an appeal. Thus question (3) is answered by affirming alternative (a).

Courts with a jurisdictional limit on the recovery of costs have grappled with how to apply section 80 and the decision of *Dimitriou*. We note the comments of Heilpern LCM in *The Owners – Strata Plan No 2795 v Luke Conrad and Natasha Grace*<sup>20</sup> when considering a matter in the Small Claims Division of the Local Court where enforcement expenses brought the amount claimed above the division's jurisdictional limit:

Prior to dealing with these submissions in detail, it is appropriate to make a comment on the difficulties obviously encountered by the current motion for practitioners, Assessors and Magistrates. Put simply, this is an area that cries out for legislative reform to clarify the situation in small claims matters. There are difficult policy issues to be determined. On the one hand, it is arguable that owners corporations should not be in any stronger position with respect to costs in the small claims division than other litigants. On the other hand, it is difficult to see fairness in a situation where a recalcitrant unit holder pays their contributions during litigation and the other unit holders must bear the burden of the outstanding legal costs. However, should parliament not act, then lawyers seeking to recover contributions will be left with little choice but to test the waters with different types of pleadings that seek to comply with the latest judicial finding from Assessors to Judges of the Court of Appeal.

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<sup>20</sup> [2009] NSWLC 21 at [29]

Legal Aid NSW is concerned that the new Bill could be interpreted to read down *Dimitriou* and submits that section 86(2) should be amended to make it clear that any orders for interest or enforcement costs must be obtained in the same proceedings as those recovering unpaid levies. We also suggest that costs should be limited to the jurisdictional limit of the relevant Court of Tribunal.

#### *Obtaining information about enforcement expenses*

Legal Aid NSW assists people who have difficulty understanding what constitutes the total amount claimed due to the lack of disclosure about enforcement expenses. This can be difficult even when legal representation is provided.

#### **Case Example 5: disclosure of enforcement expenses**

In the matter of case example 2, the owners corporation made it incredibly difficult for the client to know exactly how much he had to pay. This did not improve with the intervention of a solicitor on the client's behalf.

The owners corporation's solicitor regularly advised that "interests and costs" would be added to the levies and that these were accruing due to the protracted negotiations, but could not be precise about a figure.

Only two weeks after the matter settled the client was served with a new notice of \$1,500 in unpaid levies that accrued during the period that the parties had been negotiating. This effectively put the client back where he started, owing \$1,500 with no means of paying the levies and having to negotiate another payment plan with the owners corporation, which process in itself accrues costs.

This lack of transparency makes it very difficult for owners to understand their obligations and make arrangements to get back on track.

#### *Ensuring that payments are made to current levies before enforcement expenses*

Legal Aid NSW assists people who continue to be in arrears on their levies despite making payments. This occurs when payments are allocated first to enforcement expenses incurred by a managing agent rather than the outstanding levies, and can give rise to fresh legal proceedings against an owner for new unpaid levies, setting off another round of increasing enforcement expenses and legal costs. Where an owner is unable to keep up with ongoing levies and pay off arrears, they can be trapped in a debt spiral from which they cannot exit.

The importance of this issues is highlighted by Lulham LCM in *The Owners Strata Plan No 56059 v MI-OK Pty Limited*<sup>21</sup>:

...to save a never ending cycle of cases involving much time and huge expense in legal costs, claims by owners corporations seeking to recover outstanding contributions have to be resolved to finality, without each case providing in itself the cause of action for a further case and that further case providing in itself a cause of action for another case. The cases could go on ad finitem.

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<sup>21</sup> [2007] NSWLC 31

## Recommendations

12. The words “reasonable” be inserted before expenses in section 86(3) of the SSMB 2015.
13. Section 86 of the SSMB 2015 be amended to include a provision that enforcement expenses must not exceed an amount to be determined by the regulations. The regulations could:
  - prescribe a fee scale establishing the maximum fees that can be charged for different elements of the enforcement expenses
  - prescribe a cap on the total amount based on the cost recovery limit for the Court of the relevant jurisdiction, and
  - Complementary provisions that entitle an owner to apply to NCAT to have enforcement costs reviewed and obtain a refund if the cap has been breached.
14. The cost of the review of enforcement costs be limited. Options may include:
  - a maximum fee prescribed by the regulations to be charged in the event that enforcement expenses are upheld, and
  - a requirement that the Managing Agent absorb the cost of the review proceedings themselves where they are found to have overcharged .
15. The Owners Corporation be required to provide, at no cost, a breakdown of the amount claimed within 7 days of a request by the Owner. This should include all the information suggested in Recommendation 9 in relation to default notices, excluding a statement that the Owners Corporation intends to commence legal proceedings if this is not applicable.
16. A Code of Practice, which includes best practice in debt collection, be adopted for all Managing Agents, not just those who are members of voluntary associations.
17. The decision of an Owners Corporation to commence bankruptcy proceedings against an owner not be delegable to a Managing Agent.
18. Payments made by owners be allocated in priority of current levies, unpaid levies then enforcement costs unless otherwise instructed by the owner.
19. Recommendations in Part C be adopted to encourage early resolution of unpaid levies disputes without the need for legal proceedings.
20. Section 86(2) of the SSMB 2015 be amended to make it clear that any orders for interest or enforcement costs must be obtained in the same proceedings as the proceedings for unpaid levies to which they relate.

## Part B - Strata Schemes Management Bill 2015 – Neighbour Disputes

### *Nature of by-law (or neighbourhood) disputes*

Legal Aid NSW assists people in relation to strata by-law disputes and neighbour type disputes. While these matters can cause a great deal of anxiety and concern for our clients, they do not typically involve courts, judgment debts and the imposition of civil penalties.

### *The use of civil penalties as compensation*

Legal Aid NSW submits that the proposal set out in section 147 of the SSMB 2015 providing for larger civil penalties to be paid directly to an owners corporation for breaches of by-laws is problematic. The imposition of civil penalties by the NCAT is:

- an inappropriate tool for managing neighbour disputes in strata living arrangements, and
- contradicts the well established legal principle that parties should not be penalised for a breach of a civil contract, but may only be required to pay compensation for loss suffered.

The policy proposition behind the amendments appears to be an attempt to allow owners corporations to be compensated for breach of a by-laws, such as damage to common property.<sup>22</sup> Legal Aid NSW supports the rights of an affected owner or the whole owners corporation to obtain compensation for a breach of a by-law, however, this is better achieved through a compensation mechanism rather than civil penalties which are not connected to the loss suffered. We also note that existing provisions in the current legislation already allow owners corporations to recover the cost of damage to common property.

Civil penalties, as their name suggests, are traditionally punitive measures to deter the most egregious breaches of civil law. They sit alongside compensation and other remedies for the affected party, and exist in the National Consumer Credit Protection Act, the Fair Work Act and the Immigration Act among others. Typically, applications to a Court for civil penalties are made by the relevant regulator, with money to be paid to the regulator or into Consolidated Revenue. An affected person can seek civil penalties, to paid to themselves, only in a narrow range of cases.

It is an established legal principle that an individual in a civil dispute can only seek damages for the amount suffered as a result of the other party's conduct<sup>23</sup>. However, under the current proposal, owners corporations could recover a penalty amount far in excess of the loss suffered in what are typically private disputes between neighbours. In circumstances where the breach of a by-law also gives rise to penalties arise under criminal laws<sup>24</sup> a civil penalty should not be imposed as well.

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<sup>22</sup> OFT Fact Sheet 'By-Law Reform' August 2015

<sup>23</sup> Recently emphasised by the HCA in *Andrews v Australia and New Zealand Banking Group Limited* [2012] HCA 30.

<sup>24</sup> s.17 *Crimes (Sentencing Procedure) Act 1999*

### *Difficulties with civil penalties being paid directly to the owners corporation*

Given that many by-law breach allegations are inextricably linked to underlying disputes between neighbours, allowing civil penalties to be paid directly to an owners corporation may enable owners corporations to misuse civil penalties to target specific owners or occupiers.

This concern is compounded by section 244 of the SSMB 2015 which provides that outstanding civil penalties are to be treated as unpaid levies. If changes are not made to debt recovery practices as outlined above, this could have the effect of pursuing a civil penalty for a minor breach of a by-laws instead of negotiating or using the mediation services funded by the Office of Fair Trading. It is foreseeable that this could lead to owners being made bankrupt over what are essentially neighbour disputes.

Further, the expanded jurisdiction for owners corporations to seek a penalty against an occupant in the NCAT for breach of a by-law could be onerous, and may attract a penalty that is disproportionate to the substance of the breach and lead to an increase in disharmony and legal disputes among people living in strata housing arrangements.

### *Impact on vulnerable owners and tenants*

NSW penalty units are currently set at \$110. Under the proposed section 147 of the SSMB 2015, penalties of up to 20 units or \$2200 per breach can be imposed by the NCAT.

This is a significant amount of money, particularly for elderly or disabled residents or others who may be managing on a limited income. Legal Aid NSW submits that these new laws may cause financial hardship, especially to those who may be vulnerable or otherwise disadvantaged.

It seems reasonably foreseeable that this reform will adversely impact on the elderly and those people living with mental illness, where there might have been greater tolerance for such conduct in the past. Moreover, when read in conjunction with Part 7 of the SSMB 2015, section 147 may also present an opportunity for some strata managers to engage in aggressive debt collection activity.

### *Allowing further applications for civil penalties without issuing a subsequent notice*

Providing sufficient notice to a person about potential claims against them is critical to procedural fairness and providing an early opportunity to remedy the problem. It is problematic that once NCAT has ordered a civil penalty for breach of a by-law, an owners corporation will be able to make subsequent civil penalty applications for further breaches without serving a notice to comply. In addition, no time limit is placed on this right.

Legal Aid NSW submits that the owner should always be provided with clear notice in writing of any intention to commence NCAT proceedings. Further, a Notice to Comply should not be able to be relied upon by an owners corporation for a period of 12 months after it is served.

## **Recommendations**

21. Provisions for civil penalties in section 147 of the SSMB 2015 be removed and replaced with compensation provisions.
22. In the alternative to Recommendation 21, the amount of civil penalties that may be claimed for any breach be limited to the actual damage or loss suffered as a result of the breach.

## **Part C – Strata Schemes Management Bill 2015 – Dispute Resolution**

Effective early internal dispute resolution is critical for the success of implementing hardship practices and minimising enforcement costs. It is an important, low cost method of resolving disputes before they escalate to NCAT or formal mediation. The use of internal dispute resolution in other sectors, such as financial services, energy and telecommunications, has proven to be an effective means of resolving disputes early with minimal cost to all parties.

Section 214 of the SSMB 2015 provides that “an owners corporation may establish, by any means it thinks fit, a voluntary process for resolving disputes.” Legal Aid NSW supports the establishment of an internal dispute resolution (“IDR”) mechanism. However, IDR is unlikely to be successful unless it is mandatory and involves a clear, easy to use process.

Legal Aid NSW supports establishing a mandatory internal dispute resolution process. This could be based on the best practice modelling in the ASIC Regulatory Guide 165 and tailored to suit the strata setting. In our view this would generate enormous benefits by:

- encouraging owners corporations and occupiers to work together to resolve their own issues
- diverting matters that can be resolved internally away from the government funded mediation service, and
- diverting matters away from litigation in the NCAT.

Model processes could be set out in the regulations, with variations taking into account the size of the strata scheme and whether a managing agent is appointed. Legal Aid NSW sees this as an important “base line” initiative that could generate significant savings for the justice system and benefits to those living in strata housing.

In the event that internal dispute resolution remains voluntary, Legal Aid NSW submits that model voluntary IDR processes should be set out in the Regulations for ease of adoption into by-laws for Owners Corporations that wish to do so.

### **Recommendation**

23. Establish a mandatory internal dispute resolution practice, with model processes outlined in the regulations.

## Part D – Strata Schemes Management Bill 2015 – other matters

### 1. Building Defects

Legal Aid NSW provides advice to people who are concerned about building defects in new strata plans, especially where the client believes that the builder should make a claim on their insurance within the statutory limitation period but has not done so, with the result that the Owners Corporation will eventually have to pay the costs to fix the defect or sue the builder directly if still within the limitation period. Legal Aid NSW submits that proposal to truncate the limitation period under Part 11 of the SSMB 2015 will compound this problem, and supports the comments of the Owners Corporation Network<sup>25</sup> on this issue.

### 2. Proxies

Legal Aid NSW provides advice to people who report concerns about the bona fides of the Strata Committee decision making process. The concerns are in the nature of conflict of interest and a lack of ‘arm’s length’ decision making, and primarily arises from the influence of strata managers and building managers who hold proxies which effectively cede control of the Owners Corporation to these persons.

Legal Aid NSW supports changes to section 25 of the SSMB 2015 which clarify the proper use of proxies in meeting procedure and otherwise set limits on the powers of strata managers and building managers regarding proxies and tenure of those roles.

## Part E - Strata Schemes Development Bill 2015 – Termination of Strata Schemes

Legal Aid NSW submits that the proposal in Part 9 of the SSDB 2015 to reduce the threshold for termination of strata plans from 100% to 75% is problematic, especially for people who are vulnerable or disadvantaged. An outcome of making it easier to terminate a strata scheme will be that older strata blocks become a less secure form of housing because owners and developers will be more able to pursue opportunities to profit from termination of a scheme. As a result, older or vulnerable people will be at greater risk of losing their home, and the dislocation of being forced to leave one’s home after many years will have adverse social and financial consequences. While the SSDB 2015 proposes that owners who lose their dwelling as a result of termination of a strata scheme will be compensated in line with the provisions of the *Land Acquisition (Just Terms Compensation) Act 1991*, these provisions will not compensate for the adverse social and financial consequences of dislocation.

Owners in older unit blocks without any savings or the ability to obtain a loan to purchase alternative housing in the same area are at particular risk, as they will have no option but to move away from their support networks to a more affordable area, or enter the insecure rental market. In addition, long term tenants will suffer similar dislocation with no recourse to just terms compensation.

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<sup>25</sup> “New laws bad news for apartment owners, strata advocate says” Leesha McKenny *Sydney Morning Herald* 28 Sept 2014

### *Options to safeguard older or vulnerable owners*

Legal Aid NSW submits that further research should be conducted to properly assess the impact of these changes on older and vulnerable people. This research could also consider appropriate compensation measures such as establishing a compensation scheme that is based on the likely cost of buying a similar property in a similar location, rather than the market value of the unit in the strata scheme.

### *Proposed advice and advocacy services*

Legal Aid NSW supports the proposed “Strata Renewal Advice and Advocacy Program” and additional advice and advocacy for vulnerable owners. However, we note that the principle aims of these services is to:

- assist owners to understand any proposal to terminate the scheme and evaluate their options, and
- assist with the transition of vulnerable people from their home into institutional or other living arrangements.<sup>26</sup>

Legal Aid NSW is concerned that it could be difficult to achieve this second objective without stronger compensation provisions enabling affected owners to exercise a choice about alternative housing options.

Legal Aid NSW would welcome the opportunity to discuss how advice services could best meet the needs the vulnerable clients.

### **Recommendations**

24. Conduct a comprehensive study about the likely effects of the proposed termination provisions on older and vulnerable owners.
25. Consider alternative compensation arrangements for affected owners such as compensation based on the cost of equivalent housing rather than market value of the existing plus moving cost.

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[http://www.fairtrading.nsw.gov.au/ftw/About\\_us/Have\\_your\\_say/Review\\_strata\\_community\\_scheme\\_laws/Collective\\_sale\\_and\\_renewal\\_reforms.page?>](http://www.fairtrading.nsw.gov.au/ftw/About_us/Have_your_say/Review_strata_community_scheme_laws/Collective_sale_and_renewal_reforms.page?>)

## Part F – Recommendations

### Part A - Strata Schemes Management Bill 2015 – Unpaid Levies

1. The strata scheme provide statutory protection where owner occupiers are unable to meet their obligations temporarily due to unemployment, illness, family breakdown or other reasonable cause. Options should include one or any combination of:
  - postponing the due date of a payment or payments
  - reducing the amount required to be paid for a period of time
  - a payment plan to catch up on unpaid or postponed levies
  - waiving or reducing penalty interest and enforcement expenses, or
  - any other arrangement that will enable the owner to meet their levies obligations in the future.
2. The regulations establish a process for dealing with hardship applications, including an internal dispute resolution mechanism.
3. While a request for a variation is pending or approved, penalty interest should not accrue on the unpaid levies and debt collection activity should remain on hold.
4. Application under hardship provisions if rejected can be referred to NCAT for a determination.
5. The cost of dealing with hardship applications is not to be considered as an enforcement expense under section 86 of the SSMB 2015.
6. In relation to special levies:
  - the hardship process also apply to the imposition of special levies, where the payment of those levies would cause substantial hardship, and
  - OFT consider establishing a no interest loan scheme to assist low income owners to meet the cost of special levies in a timely way.
7. Amendments be made to the SSMB 2015 to establish a process to assist owners if they must rent elsewhere due the unit being uninhabitable as a result of an act or omission of the owners corporation. Options include:
  - Specifying that owners may seek orders in the NCAT for compensation for loss suffered in these circumstances
  - Requiring an owners corporation to claim on their building insurance to cover the cost of the owner’s rental accommodation
  - Suspending the requirement for the owner to pay levies for the period in which the unit is uninhabitable, or
  - Entering into hardship arrangements enabling levies to be paid during the period in which the unit is uninhabitable.
8. Explore options for specific measures to provide compensation for an owner whose property is uninhabitable as a result of an act or omission of the owners corporation.

9. Section 86 of the SSMB 2015 be amended to require an owners corporation to issue a notice in writing before commencing legal proceeding with the following information:
  - the total amount due
  - the components of this amount – levies, interest and enforcement costs
  - a statement that legal proceedings will commence if the amount is not paid within 30 days
  - a statement of any new amounts that will also become due within the 30 days, and
  - a statement that if the person is experiencing financial hardship they may seek assistance from the Financial Counselling Hotline by phoning 1800 007 007.
10. The form of this notice be prescribed in the Regulations.
11. If our recommendations in Section 1 of Part A above are adopted, information is provided about how to make a hardship application.
12. The words “reasonable” be inserted before expenses in the section 86(3) of the SSMB 2015.
13. Section 86 of the SSMB 2015 be amended to include a provision that enforcement expenses must not exceed an amount to be determined by the regulations. The regulations could:
  - prescribe a fee scale establishing the maximum fees that can be charged for different elements of the enforcement expenses, and
  - prescribe a cap on the total amount based on the cost recovery limit for the Court of the relevant jurisdiction.
  - Complementary provisions that entitle an owner to apply to NCAT to have enforcement costs reviewed and obtain a refund if the cap has been breached.
14. The cost of this review of enforcement costs be limited. Options may include:
  - a maximum fee prescribed by the regulations to be charged in the event that enforcement expenses are upheld, and
  - a requirement that the Managing Agent absorb the cost of the review proceedings themselves where they are found to have overcharged.
15. The Owners Corporation be required to provide, at no cost, a breakdown of the amount claimed within 7 days of a request by the Owner. This should include all the information suggested in Recommendation 9 in relation to default notices, excluding a statement that the Owners Corporation intends to commence legal proceedings if this is not applicable.
16. A Code of Practice be adopted for all Managing Agents, which includes best practice in debt collection, not just those who members of voluntary associations.

17. The decision of an Owners Corporation commence bankruptcy proceedings against an owner should be not be delegable to a Managing Agent.
18. Payments made by owners be allocated in priority of current levies, unpaid levies then enforcement costs unless otherwise instructed by the owner.
19. Recommendations in Part C be adopted to encourage early resolution of unpaid levies disputes without the need for legal proceedings.
20. Section 86(2) of the SSMB 2015 be amended to make it clear that any orders for interest or enforcement costs must be obtained in the same proceedings as to the proceedings for unpaid levies to which they relate.

#### Part B - Strata Schemes Management Bill 2015 – Neighbour Disputes

21. Provisions for civil penalties in section 147 of the SSMB 2015 be remove and replaced with compensation provisions.
22. In the alternative to Recommendation 21, the amount of civil penalties that may be claimed for any breach be limited to the actual damage or loss suffered as a result of the breach.

#### Part C - Strata Schemes Management Bill 2015– Dispute Resolution

23. Establish a mandatory internal dispute resolution practice, with model processes outlined in the regulations.

#### Part D – Strata Schemes Management Bill 2015 – Other matters

Nil recommendations.

#### Part E – Strata Schemes Development Bill 2015 – Termination of Schemes

24. Conduct a comprehensive study about the likely effects of the proposed termination provisions on older and vulnerable owners.
25. Consider alternative compensation arrangements for affected owners such as compensation based on the cost of equivalent housing rather than market value of the existing plus moving cost.