STRATA KNOWLEDGE

At the Crossroads: Addressing Pervasive Conflicts of Interest in Strata Management

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This report is dedicated to the memory of Gary Bugden OAM. Gary's expertise, dedication and tireless advocacy have left an indelible mark on the strata sector and will continue to inform the work of practitioners and researchers to come. His insights, referenced in this report, stand as a testament to a life devoted to excellence in law and service to the community.

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Report Summary

This report investigates systemic conflicts of interest within the Australian strata management industry, a sector currently transitioning from an occupational to a professional model. Prompted by heightened media scrutiny and regulatory debate following major exposés in 2024, the research aims to empirically identify the relationships and practices that generate conflicts of interest, evaluate current mitigation strategies, and assess their impact on strata lot owners.

The study employs a qualitative, mixed-methods approach, including analysis of 153 strata management company websites, review of 35 management agreements, in-depth interviews with 20 senior strata managers, and engagement sessions with 16 strata lot owners. This triangulated methodology enables a comprehensive exploration of industry practices, regulatory frameworks, and stakeholder experiences.

Findings reveal that conflicts of interest are deeply embedded in the industry's business models, particularly through insurance commission dependencies, developer consulting arrangements, vertical integration with affiliated entities, staff remuneration structures tied to additional service fees, and supplier referral relationships. Disclosure, the primary regulatory tool, is shown to be ineffective, often creating an illusion of transparency while failing to address underlying ethical risks or restore trust. Owners frequently lack understanding of commission structures, cross-subsidisation effects, and the true nature of affiliated relationships, leading to widespread distrust and agency problems.

The report identifies three categories of industry participants: traditional commission-dependent operators, reform-oriented operators who have adopted ethical fee-for-service models, and transition operators awaiting legislative mandates. It concludes that voluntary reform is unlikely to succeed due to entrenched competitive pressures and recommends comprehensive legislative intervention. Key policy recommendations include banning insurance commissions (including for insurance brokers), prohibiting initial management appointments for companies providing developer consulting, restricting affiliated entity dealings, and reforming delegated authority processes.

Ultimately, the report argues that only robust regulatory reform, supported by industry leadership and consumer education, can restore integrity and trust in strata management. The transition will be disruptive but is both necessary and achievable, with early adopters already demonstrating the viability of ethical, transparent business models.

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Introduction

The strata management industry is at a critical juncture in its evolution. It is on the precipice of changing from an occupational-based industry to a professional one. However, conflicts of interest are critical obstacles that must be overcome to move the industry forward. There are commonplace practices and relationships that are at odds with fundamental legal and ethical duties owed by strata managing agents to their clients. Decades of simmering concerns erupted in 2024 under a barrage of media attention exposing the underbelly of the strata management industry. Since then, regulators and commentators have been debating these conflicts of interest. This together with the increased media scrutiny has enlightened strata lot owners of these practices which has led to a growing distrust of the industry as a whole.

Change is required but it can't be achieved until there is a better understanding of the phenomenon at the centre of the debate. It is imperative that empirically-based research is undertaken that examines conflicts of interest in the strata management industry. The purpose of this research is to identify the types of relationships and practices that give rise to conflicts of interest, the processes and procedures that management companies implement to manage or prohibit these conflicted arrangements (if any), and the effects these arrangements have on strata owners. This investigation will enable strata managers to understand the relationships and practices that conflict with their legal duties, ethical obligations and those impacting the professional standing of the industry.

The paper is presented in three parts. Part 1 provides an overview of the types of risky dealings previously reported. This is followed by a review of conflicts of interest as a concept and then mitigation and management strategies are outlined and reviewed including the effectiveness of information disclosure. Part 2 outlines the methodology approach undertaken and the findings from four phases of inquiry. Part 3 discusses the findings, draws conclusions and makes recommendations for government and the strata management industry.

Part 1: Conflicts of interest in context

1.1 Raising the conflict of interest risk: a historical account

On 21 March 2024, the ABC started reporting on conflicts of interest in the strata management industry.[1] During the year, more detailed investigations were undertaken culminating in a Four Corner's episode titled 'The Strata Trap'.[2] For many working in the strata sector, the practices and relationships highlighted in these stories were unsurprising.

A litany of research papers, reports and legal cases over several decades have highlighted conflict of interest risks in the strata management industry. In essence, this is not a new topic of discussion but it marks the first time a sustained debate has occurred within the strata sector under regulatory attention.

The following provides a brief historical overview of the conflict of interest risks in the strata management industry. The list is not exhaustive but illustrates the concerns raised over decades but ignored.

[1] Linton Besser and Ninah Kopel 'High-profile strata company Netstrata caught charging excessive fees and taking kickback' *ABC News* (online 21 March 2024) https://www.abc.net.au/news/2024-03-21/netstrata-strata-charging-excessive-fees/103609380.

[2] Linton Besser 'Exorbitant fees and undisclosed kickbacks: Inside the poorly regulated strata management' *ABC News* (online 2 April 2024) https://www.abc.net.au/news/2024-04-02/fees-and-kickbacks-poorly-regulated-strata-managment-industry/103654322; Linton Besser 'The Strata Trap' *Four Corners* (Australian Broadcasting Corporation, 2024) https://www.abc.net.au/news/2024-09-09/the-strata-trap/104330248.

In August 1992, the Sydney Morning Herald published several articles under the broad heading, Strata Homes: Hidden Cost Scam.[3] The articles exposed conflicts of interest and concerning practices and relationships relating to Alliance Strata Management. As is often the case, several savvy and disgruntled lot owners embarked on their own investigations uncovering undisclosed commissions and affiliated relationships. Through a parent company, Alliance had created subsidiary companies including an insurance broking firm, a repairs and maintenance company, and a compliance company that created sinking fund [capital works] forecasts. On the day these articles were published, the Real Estate Services Corporation (the relevant licensing body at the time) commenced a prosecution of Alliance and its Director John Scott alleging the failure to disclose commissions was a breach of the relevant Act. The underlying argument being that both the entity and Scott were not 'fit and proper persons' to hold a licence.[4] This prosecution led to several years of litigation.[5]

A side article titled: 'How big budgets can tempt managers', provided further insight into common problematic practices. A strata manager described his experience of being offered kickbacks. He said painters were the worst offenders offering up to $1000 cash to secure a job. Some banks offered a 1% secret commission to move accounts, insurance companies offered up to 25% in commissions, and there was constant overcharging by suppliers and service providers.[6]

In a book about strata title in New South Wales, the author cites a letter written in 1994 by the board of the Institute of Strata Title Management (ISTM) to its members after the conclusion of the Alliance case. The letter stated the board was considering the phase out of insurance commissions.[7] Thirty years later, Strata Community Association (NSW) (the successor of ISTM) announced that from 2026 new Strata Community Association (NSW) issued contracts would not include an option to accept insurance commissions, effectively taking a policy position to phase out insurance commissions.[8]

In 2008, well-known strata lawyer Gary Bugden, wrote an article chronicling the history of the strata management industry revenue model dating back to the 1970's.[9] He explained the competitiveness of the market at the time with 'backyard operators' marketing their management services at very low fees. With little changing in the subsequent decades, Bugden discussed how the industry responded by finding new revenue streams and charging for extra services. He cautioned the strata management industry and set out the numerous legal obligations that applied including the fiduciary duty and the secret commission provisions stipulated in state criminal laws. He drew this conclusion:

> Despite the best efforts of legal draftspersons who craft the terms of standard strata management agreements, from a business risk management perspective, strata managers would be well advised to seriously reduce the services used to generate revenue outside the annual fees per unit charge. Inevitably, this will drive a need to increase the annual fees per unit. However, this may well be an opportunity rather than a treat if it is marketed positively and

[3] Ben Hills, 'Strata Homes Hidden Cost Scam: At your service – for a sky-high price', *Sydney Morning Herald* Sydney (Sydney, 12 August 1992) 4.
[4] John Coleman, *From the Ground Up: The Story of Strata Title in New South Wales* (Strata Community Association (NSW), 2021) ch 5.
[5] *Real Estate Services Council v Alliance Strata Management Ltd* (1994) NSWCA 258.
[6] Ben Hills, 'How big budgets can tempt managers', *Sydney Morning Herald* (Sydney, 12 August 1992) 4.
[7] Coleman (n 4) 74.
[8] Liam Kerr, '*SCA (NSW) to Phase Out Strata Insurance Commissions'* (Blog post, 2 September 2025) https://scansw.com.au/news/sca-nsw-to-phase-out-strata-insurance-commissions.
[9] Gary Bugden, 'Strata Management Revenue Model – Sustainable? (Discussion Paper, 2008) https://bagl.com.au/research-papers/.

> pampers the current market dissatisfaction with "hidden extras" in strata management agreements. It is also a better revenue model from a straight business perspective.[10]

This advice was not taken, and the strata management industry continued for decades to both ignore its legal duties and offer low per lot management fees, subsidising revenue using various methods.

In 2011, the author of this paper, presented preliminary research findings to the strata sector on conflicts of interest with a particular emphasis on the relationship between property developers and strata managers. The presentation emphasised the legal risks faced by the strata management industry in continuing to undertake developer consulting work for free in exchange for management appointments and other benefits.[11]

In 2017, the Australian Government directed the Australian Competition and Consumer Commission (ACCC) to conduct an inquiry into the supply of residential insurance in Northern Australia. Strata insurance was one area of focus. Although the scope of the inquiry was extensive and the inquiry took three years to complete, one of the significant findings related to conflicts of interest in the strata management industry.[12] Specifically, the investigators determined that conflicts of interest were common and recommended that state and territory legislation be amended to prohibit strata managers from accepting commissions in relation to arranging insurance.[13] The report suggested that:

> Strata managers should be required to negotiate any fees or payments for arranging insurance directly with the body corporate they are servicing. This would encourage remuneration arrangements that better align the interests of the strata manager and their clients.[14]

In 2021, Bugden detailed the inherent problems that arose when strata managers ignored their fiduciary duty. He set out the fiduciary duty, how the duty was applied, and the risky dealings that strata managers needed to avoid. For Bugden, 'risky dealings':

> Involve arrangements that do not directly amount to a manager accepting or paying a consideration for a personal benefit which is or may be detrimental to their principal, but which rather indirectly amounts to such an outcome.[15]

For Bugden, some of the risky dealings included: "free or discounted goods and services; complimentary training and continuing professional development services; free developer consulting; sponsorship; and advertising arrangements."[16] Again, Bugden cautioned the strata management industry to avoid risky practices and when they couldn't avoid them, to manage them carefully. He emphasised the need to restrain from "pushing indirect income boundaries to the limits"[17] and adopt a more professional approach with transparent practices.

This brief overview illustrates that compromising practices and relationships have plagued the strata management industry for well over three decades and conflict of interest risks have been advised on numerous occasions but not resulted in any changes to industry practice.

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[10] Ibid 4.
[11] The presentation was based on research outcomes detailed in: Nicole Johnston, 'An Examination of How Conflicts of Interest Detract from Developers Upholding Governance Responsibilities in the Transition Phase of Mult-Owned Developments: A Grounded Theory Approach' (Thesis, Griffith University, 2017).
[12] Australian Consumer and Competition Commission, *Northern Australian Insurance Inquiry* (Final Report, November 2020).
[13] It should be noted that the investigators also recommended that insurance brokers should be prohibited from accepting commissions.
[14] Australian Consumer and Competition Commission (n 12) 22.
[15] Gary Bugden, 'Strata Managers as Fiduciaries' (Discussion Paper, 2021) https://bagl.com.au/research-papers/.
[16] Ibid 8.
[17] Ibid 11.

1.2 High conflict of interest risk industries

Strata management practitioners have consistently questioned why their industry is being targeted, particularly by the media. The short answer is the complexity of the strata environment, the agency relationship and the reliance on external services means that there is a higher risk of conflicts of interest occurring. It is important to note that conflict of interest risks are not limited to strata management. Legal, medical, and financial industries are also often in the spotlight.

Conflicts of interest are more prevalent in environments where the service or product being offered is complex. This is because of the increased opportunity for the duty-bound person (e.g. manager) to ignore their obligations and cheat or lie without being detected.[18]

In the strata environment, specialised exchange is inherent. The complex legal framework, the prescriptive nature of strata legislative provisions, volunteer committee members, the nature of the agency relationship, apathetic lot owners, and the underlying strata structure have created an environment where owners corporation members rely heavily on strata managers. Owners corporation clients need to trust their manager to guide them through a complex web of compliance and interpersonal challenges. A vulnerability exists because strata law, governance and management are rarely their area of expertise.

Special legal regulations are imposed on specific occupational groups that 'have the greatest opportunities to cheat without detection and whose cheating imposes the most serious cost on others.[19] Stakeholders (including developers, strata managers, owners corporation committees, caretakers/building managers) are subject to regulations that, inter alia, attempt to negate the harmful effects of conflicts of interest. When the managing agent also has delegated authority to undertake certain functions or has been appointed as an administrator for the owners corporation, the risks are even higher as client oversight is more limited. Further care and regulatory oversight is required in these situations.

Strata managing agents must understand how to navigate these ethical and legal risks so they can recognise when a conflict of interest situation arises. However, in order to do this successfully the concept must be defined to improve their understanding.

1.3 Conceptualising conflicts of interest

It is essential in discussions about conflicts of interest to define the concept. A consistent definition of 'conflicts of interest' should be articulated in the law and codes of ethics but this is a rarity. Parties who are assigned certain duties in a particular role need to understand what they can and cannot do. If there is no working definition, parties determine their own response to a situation which can increase the risk of conflicts of interest occurring.

Unfortunately, there is not one agreed upon or succinct definition. Although prominent scholars, like Carson and Villaran[20], appear to be nearing a definition consensus, what is witnessed in general commentary is a mishmash of definitions that are usually either too narrowly focused or too wide. As a result, discussions relating to conflicts of interest are often misguided.

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[18] Alison G Anderson, 'Conflicts of Interest: Efficiency, Fairness and Corporate Structure' (1978) 25 UCLA Law Review 738.
[19] Ibid.
[20] Thomas L Carson, 'Conflicts of Interest' (1994) 13 Journal of Business Ethics 387, 388; Alonso Villaran, *The Ethics of Conflicts of Interest in Business: An Introduction* (Rowman and Littlefield, 2021).

Before determining a good working definition, it is just as important to highlight what does not constitute a conflict of interest. This will help frame the discussion and conceptualisation.

Conflicting interests and conflicts of interest are not the same. Interests may collide regularly that don't constitute a conflict of interest. A good example is two lot owners who vote differently at a general meeting in their own but opposing interests. This is not a conflict of interest.

In terms of a workable and well-articulated definition, a favoured conceptualisation is:

> *A conflict of interest is a situation in which an **interest tempts one** to disregard a work-related **duty** – a situation that threatens the interest of **someone else.***[21]

It is useful to break down this definition to understand who the parties are and in what circumstances the conflict of interest might arise.

1. The **nature of the relationship** - which is based on reliance and trust. It is often the case where one party is a professional or agent of another (strata manager) and the other is a client or more vulnerable party (owners corporation).

2. **Obligation or duty to act** in a certain way - determination of the duty or obligation needs to be undertaken. This means looking for either an elevation of the reliant party's interests ("best interests") or a displacement of the professional's own interest ("fiduciary"). These duties often arise in law (both statutory and general law), in contracts or in codes of ethics.

3. The **interest** - can be tangible or intangible, harming and promoting. Interest should be interpreted broadly and not be limited to financial and other common beneficial interests. This is broader than just conflicted remuneration.

4. The **temptation –** the duty-bound person only needs to be tempted not necessarily concede or give in to the temptation. A conflict of interest arises when a person simply has difficulty discharging their duty. It is also important to note that the interest might relate to the promotion of a third party's interest. For example, where the interests of a property developer or affiliated entity are elevated by a strata manager over the interests of the owners corporation.

Deconstructing this definition, it is evident the threshold for what constitutes a conflict of interest is low. This definition captures most, if not all, commercial transactions where a duty-bound party is confronted simultaneously with their professional responsibility and their personal interest.[22]

It is important to recognise that being in a conflict of interest situation is not necessarily wrong.[23] When a party only needs to be tempted to disregard their duty (not ignore it all together) to be in a conflict of interest, the harm or breach is inconsequential as no action has been undertaken. Further, a duty-bound person is sometimes placed in a conflict of interest situation without it being their fault and maybe against their will. The temptation might be

[21] Alonso Villaran, *The Ethics of Conflicts of Interest in Business: An Introduction* (Rowman and Littlefield, 2021) 59.
[22] Don A Moore and George Loewenstein, 'Self-Interest, Automaticity, and the Psychology of Conflict of Interest' (2004) 17(2) Social Justice Research 189.
[23] Villaran (n 21).

fleeting and the duty-bound person may take immediate steps to thwart any action that may result in them being unable to discharge their duty.[24]

The real problem arises after the duty-bound person is confronted by a conflict of interest situation. It is their next steps that determine the level of legal and ethical risk exposure. Legal risk can be mitigated if the duty-bound person complies with rules regulating the conflict of interest. Ethical risk may not be so easy to mitigate.

1.4 Regulating conflicts of interest in strata management

There are several legal sources that regulate strata-related conflicts of interest. Some are purposely aimed at regulating strata managers; others broadly cover occupational groups or individuals where a principal and agency relationship exists. From a statutory perspective, these regulations can be generally found in strata-related legislation and state-based crime legislation. From a common law perspective, the equitable doctrine of fiduciary imposes a legal obligation aimed at preserving the sanctity of the principal/agent relationship.

As highlighted in the previous section, it is essential to determine the sources of the obligations or duties to act in a certain way when assessing whether a conflict of interest has arisen. The following provides a brief overview of these laws.

1.4.1 Strata-related regulations

Most Australian states and territories legally impose either directly or impliedly 'best interest' duties on strata managing agents. The phrasing and orientation of the duties differ across jurisdictions. Some predominantly apply positive obligations (to act in a certain way), others apply negative obligations (to restrain from acting in a certain way). Queensland falls into the former category imposing a duty to act in the best interest of the body corporate unless unlawful to do so.[25] Victoria, Western Australia and South Australia largely fall in the latter category where the obligation is not to use their position (or information) to gain an advantage or cause a detriment.[26] South Australia is the only state reviewed that embeds the common law duty of fiduciary (a negative obligation) into the legislation.

New South Wales is slightly more convoluted. Firstly, it is evident that the strictness (with penalties applying) of section 57 (1) and (2) of the *Strata Schemes Management Act 2015* implies a best interest duty. Subsection 2, is the overarching provision and states:

> A strata managing agent must not, in connection with the provision of services as a strata managing agent or the exercise of functions as a strata managing agent, request or accept a gift or other benefit from another person for himself or herself or for another person.

A similar implied duty is expressed in the *Property and Stock Agents Act 2002*, an Act regulating strata management agents (as licensees) and its accompanying regulation.[27] The relevant provision in the Act (s. 55) states that:

[24] It is worthwhile to point out that some make the distinction or classify conflicts of interest as; apparent or real, and potential or actual. These distinctions simply muddy the waters as a potential conflict of interest is a situation that may or may not present itself. All a duty-bound person can do is prepare for something that may or may not eventuate. An apparent (as opposed to real) conflict of interest is often deemed as a conflict with no interest or where the right kind of duty does not exist. Therefore, it is not a conflict of interest but perhaps a moral problem.
[25] *Body Corporate and Community Management Act 1997* (Qld), sch 2 cl 4.
[26] *Owners Corporations Act 2006* (Vic), s 122; *Strata Titles Act 1985* (WA), s 146(1)(d),(e); *Strata Titles Act 1988,* s 27(C).
[27] *Property and Stock Agents Regulation 2022* (NSW).

> A licensee is not entitled to any commission or expenses from a person for or in connection with services performed by the licensee in the capacity of licensee for or on behalf of the person unless…the services were performed pursuant to an agreement in writing.

The relevant provision in the regulation (sch. 1, r. 12) is geared toward regulating service provider referrals ensuring a level of independence.

> An agent who refers a person to a service provider must not falsely represent to the person that the service provider is independent of the agent. A service provider is independent of an agent if the agent receives no rebate, discount, commission or benefit for referring a client or customer to the service provider, and the agent does not have a personal or commercial relationship with the service provider.

In addition, supervision guidelines have been issued requiring principal licensees to establish operational procedures to ensure compliance. To mitigate or eliminate conflict of interest risks, part 2.5.2.2 requires the maintenance of:

> A register of gifts and benefits accepted or declined while carrying out functions as a licensee or certificate holder, as well as details of the nature and value of the gift or benefit and who made and received the offer, and a procedure for how to comply with any disclosure obligations related to conflicts of interest that apply under the Act or the *Strata Schemes Management Act 2015*.

These supervision guidelines are enforceable with penalties applying for non-compliance.

1.4.2 Crime-based regulations

More stringent and serious penalties apply under the relevant crime-based regulations in each state and territory. The relevant provisions in each jurisdiction are similar and focus on secret commissions.[28] The *Crimes Act 1900* (NSW) (s. 249B) states:

> If any agent corruptly receives or solicits (or corruptly agrees to receive or solicit) from another person for the agent or for anyone else any benefit as an inducement or reward for or otherwise on account of doing or not doing something, or having done or not having done something, or showing or not showing, or having shown or not having shown, favour or disfavour to any person, in relation to the affairs or business of the agent's principal, or the receipt or any expectation of which would in any way tend to influence the agent to show, or not to show, favour or disfavour to any person in relation to the affairs or business of the agent's principal, the agent is liable to imprisonment for seven (7) years.

Similarly worded provisions apply to anyone who corruptly gives or offers to give an agent any benefit.[29]

Under this legislation, an agent is broadly defined as any person employed by, or acting for or on behalf of, any other person in any capacity.[30] It is a low threshold and undoubtedly strata managers fall under this definition.

1.4.3 Equitable doctrine of fiduciary duty

In many regulated business environments, practitioners often focus on the laws that relate to their industry or work. Often these laws are more digestible as they are succinctly packaged in a document downloadable from numerous online sources. Industry association bodies usually provide legal updates and guidance as these laws change and impact their members. Occasionally, common law rules or doctrines are bandied about with little appreciation of the

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[28] *The Criminal Code 1899* (Qld), s 442B, 442BA; *Crimes Act 1958* (Vic), s 176; *The Criminal Code 1913* (WA), s 529, 530.
[29] See *Crimes Act 1900* (NSW) s 249B(2).
[30] *Crimes Act 1900* (NSW) s 249A.

potential ramifications for breaching these rules. The equitable doctrine of fiduciary is one such doctrine that, arguably, has been systematically ignored in the strata management industry.

Fiduciary duty is grounded in a long history and is the highest duty owed in law.[31] If a person is deemed to be a fiduciary, they have a strict obligation to exclusively act in the interests of another (the principal, the client, the beneficiary, the company, the employer, or the co-partner).[32] Trust and loyalty are at the heart of fiduciary duty and so it a vital doctrine to consider when discussing conflicts of interest. The doctrine itself is relatively straightforward, a fiduciary must:

1. Not allow themself to be in a position in which their duty to their principal conflicts with their personal interest or their duty to two principals conflict = 'conflict rule'

2. Not make a profit at the expense of the principal = 'profit rule'.[33]

It is commonly accepted that strata managing agents owe fiduciary duties to their owners corporation clients. Although Bugden suggests that the role a strata manager performs is likely to be the key in determining whether a strata manager is a fiduciary.[34] That is, if the manager undertakes purely clerical type work (e.g. only keeping records) then it may be arguable they are not fiduciaries. In most, if not all, current management arrangements, the work performed by managers is beyond pure clerical work.

Of course, a fiduciary, can be paid for the work performed and the profit made from their business (if applicable). The issue is if the profit made is at the expense of the client.

These best interest duties embedded in various legal sources showcase not only the sanctity of the special relationship that exists between strata managers and owners corporation clients but the need to ensure these clients are afforded protections under the law. The need has arisen because principals are often in a more vulnerable position and the temptation to benefit from that relationship is often too great.

Now that it is apparent that strata managers owe the types of duties required when evaluating conflicts of interest, the next step is to determine what can be done when a manager is tempted by a situation and unable to discharge their duties.

1.5 Mitigating and managing conflicts of interest

Before determining whether a conflict of interest can be mitigated or managed, there needs to be an acknowledgement that the practice or relationship in question gives rise to a conflict of interest. When confronted with a conflict of interest situation, a duty-bound person can either accept or deny the existence of the conflict. In the strata context, accepting some situations (practices and relationships) give rise to a conflict of interest seems to be a challenge.

The articulation of what circumstances should put a strata manager on alert has been somewhat shielded by strata legislation. That is, policymakers have, perhaps unknowingly, created boundaries around problematic practices and relationships. The effect being that conflicts of interest that exist but are not regulated may not be on the radar of managers as being a high-risk practice or relationship. In essence, a line has been drawn in the sand about what is acceptable and what is unacceptable with little regard given to the pervasive nature or effects of these dealings. To complicate matters, each jurisdiction has drawn the line differently

[31] Cathy Sherry, 'Disclosure will not fix everything: Understanding the fiduciary relationship' (Conference Paper, Strata Impact Conference, 14 August 2025).
[32] Ibid.
[33] Johnston (n 11); Sherry (n 31).
[34] Bugden (n 15).

and created confusion regarding what constitutes a conflict of interest. This confusion does not help the management industry to acknowledge the conflicts or implement strategies to curtail the effects of these conflicts of interest.

Once a duty-bound person accepts there is a conflict, the situation can be avoided (opting out of participating in the situation) or it can be managed.

One approach to combat conflicts of interest would be to simply prohibit duty-bound people from engaging in them. In some areas of strata law, certain activities that have the potential to result in a greater level of harm have been prohibited. However, not all conflict of interest situations lead to the same level of harm or cause any harm at all. Presumably, legislatures think most conflict of interest situations can be managed to minimise any harmful effects.

The five E's is a conflict of interest management strategy developed by Villaran.[35] These strategies are presented in Diagram 1.

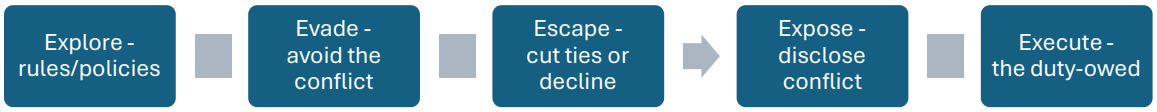

Diagram 1: Villaran's conflict of interest management strategy

For Villaran the five E's are action items for individuals to undertake when confronted with a conflict of interest. These strategies are not sequential but serve to guide individuals out of conflict of interest situations.

Explore: investigate whether organisations and occupations have established rules and policies on conflicts of interest. These might relate to laws, codes of ethics or conduct, or professional norms.[36] Not all businesses or occupations are subject to conflicts of interest or the same types of conflicts. It is important to understand how practitioners are regulated and perceived. This paper has highlighted the legal rules relevant to strata managing agents. It is important to add that the Strata Community Association (SCA) has developed a code of ethics that establishes principles (including conflicts of interest) which must be upheld by its members.[37]

Evade: if a party avoids a conflict, it will save them from all that a conflict of interest entails. Unfortunately, it is sometimes difficult to evade conflicts of interest.[38] Someone can be placed in a situation without an invitation (ie: solicitation). For example: a service provider offering a kickback for referral work.

Escape: if a party finds themselves in a conflict of interest situation (whether or not by their own volition), they must escape from it. If the party cannot recuse themselves from the duty (which is very difficult in strata as the duty is embedded in the role), divesting from the interest

[35] Villaran (n 21) 102-111.
[36] Strata Community Association, *SCA National Code of Ethics* https://www.strata.community/code-of-ethics
[37] Villaran (n 21) 102-111.
[38] Ibid.

is a good way to escape. That means cutting ties with a supplier or provider or simply declining the offer.[39]

Expose: the party must tell the principal about the situation that gives rise to the conflict of interest. This requires information disclosure. If this is the management strategy employed, the manager must communicate the conflict clearly so the client does not misunderstand the situation or fail to recognise its seriousness.[40] To be clear, exposing a conflict does not eliminate it. As will be detailed in this paper, there is empirical research that demonstrates care needs to be taken with this approach.

Execute: a manager still needs to execute their duty even after they have exposed or disclosed a conflict of interest. This is still the case when the manager has received informed consent to proceed from the client. Ethically, the manager must let go of the opportunity regardless of consent to the disclosed conflict. When a manager's judgement is compromised, they might get guidance from an external independent source to determine the best outcome.[41]

As indicated, evading or escaping conflicts of interest is the best approach. Exposing or disclosing the conflict of interest is a flawed strategy as detailed next.

1.5 Disclosure as a tool to mitigate conflicts of interest

In terms of conflicts of interest, the wrongdoing manifests when a legal or moral 'best interest' duty is breached. These duties recognise that one party is more vulnerable and so legal protections must be created to protect against corruptions or other harms. As previously discussed, trust and loyalty are at the heart of these duties, creating a promise by the duty-bound person to serve the duty-owed person and their interests. Breaking a promise can cause harm, fuel deception and distrust.[42]

Given the nature and sanctity of these duties, the strict enforcement of them would be assumed. However, the law has provided a defence, a pardon for breaching these duties. Information disclosure is consistently used as a panacea to right the wrong. This is based on the theoretical assumption that people are rational and will have the cognitive ability to digest potentially complex information, discount biased advice and make an informed and optimal decision for themselves.[43]

Rational choice theory is an economic theory based on the assumption that people 'will process information, make choices, and execute behaviours in a way calculated to maximise their expected utility; that is, to maximise the differential between expected benefits and expected costs.'[44] This assumption requires people to 'infer facts about the world by applying principles of deductive logic to all known, relevant information.'[45] Based on this assumption, policymakers' have favoured the use of information disclosures in a variety of commercial transactions.

Disclosure is an easy mechanism as it requires limited substantive change. It works well in an environment predicated on the belief that conflicts of interest are unavoidable.[46]

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[39] Ibid.
[40] Ibid.
[41] Ibid.
[42] Ibid, 85.
[43] Nicole Johnston and Karla Johnston 'The Legal Psychology of Disclosure in the Multi-owned Property Context' (Conference Paper, Australian College of Community Association Lawyers (ACCAL) Conference, 2018).
[44] Russell Korobkin, 'The Problems with Heuristics for Law' in Gerd Gigerenzer and Christoph Engel (eds), Heuristics and the Law (MIT Press, 2014).
[45] Ibid.
[46] Johnston (n 42).

For professionals facing conflicts of interest, disclosure promises minimal disruption from the status quo; it does not require them to sever financial relationships or change how they get paid. For regulators and policy makers, disclosure absolves them of some of their responsibility to limit market exploitation by transferring to duty owed persons the responsibility of looking out for themselves. And to the duty owed, disclosure promises to give them the tools they need to look out for their own interests.[47]

In the strata management context, each jurisdiction has utilised information disclosure as a regulatory tool to curtail any potential effects of conflicts of interest.[48] The way these regulations are drafted vary. Undoubtedly, New South Wales has implemented the most prescriptive disclosure regulations in the country. The *Strata Schemes Management Act 2015* (s. 60) requires specific details relating to commissions, training services, affiliated entities, connections to suppliers and original owners of relevant strata schemes to be provided in reports and notifications. Financial penalties apply for non-compliance.

Information disclosure regimes are not new. However the inclusion of conflict of interest disclosures detailing specific risky dealings are more recent. It is apparent that information disclosure is the favoured regulatory tool used to combat conflicts of interest in strata.

There is a growing body of empirical evidence that casts doubt on the use of information disclosures for this purpose and suggests the underlying theoretical assumption is flawed.

1.6 The reality of information disclosure

It is an ill-conceived proposition that by communicating a future harm, its potency dilutes or is cured completely while also absolving the person who caused the harm. Society does not usually accept such situations. However, in relation to conflicts of interest, lawmakers have misguidedly relied on and embedded a mechanism that allows just that – a cure and absolution for wrongdoing.

Numerous empirical studies have been undertaken on the effectiveness of disclosure in conflict of interest situations. The general conclusion is that "disclosure cannot generally be assumed to be an effective solution for the problems created by conflicts of interest; it may even make matters worse."[49] The reason for this is explored next.

1.7 The transparency illusion

There is an underlying premise that information disclosure achieves transparency. It is assumed that if the information is available, the people who receive it will automatically understand it and use it to make an informed decision. The linkage of these two concepts is often seen when governments create legislation where disclosure is a central feature.

A newsletter from Queensland's Office of the Commissioner for Body Corporate and Community Management stated:

[47] Daylian M Cain, George Loewenstein and Don A Moore, 'Coming Clean but Playing Dirtier: The Shortcomings of Disclosure as a Solution to Conflicts of Interest in Don Moore et al (eds), *Conflicts of Interest: Challenges and Solutions in Business, Law, Medicine, and Public Policy* (Cambridge University Press, 2010) 108.
[48] See for example, *Body Corporate and Community Management (Standard Module) Regulation 2020* (Qld) ss 155, 156, 157; *Owners Corporations Act 2006* (Vic) s 122B; *Strata Titles Act 1985* (WA) s 147; *Strata Titles Act 1988* (SA) 27D.
[49] Cain (n 46).

> Notably, the biggest update [to the legislation] was adding to existing disclosure requirements that any monetary benefits had to be disclosed to ensure transparency.[50]

From the New South Wales Minister for Better Regulation and Fair Trading, Anoulack Chanthivong:

> These [disclosure] reforms are about ensuring transparency and accountability for everyone living in strata communities.[51]

The fundamental problem is that transparency and disclosure are often conflated. There can be extensive disclosure without ever achieving transparency.

Information can be:

- Disclosed but incomprehensible (linguistic complexity)
- Disclosed but overwhelming (information overload)
- Disclosed but misleading (strategic framing)
- Disclosed but inaccessible (poor design)
- Disclosed but not useful (irrelevant content)[52]

If the actual goal of regulatory reform is to achieve transparency, then disclosure regimes need to be thoroughly assessed.

If a law only requires the disclosure of a commission, payment or benefit (that is a dollar amount or percentage) or a notice issued that stipulates a connection between third parties, then it is up to the duty-owed party to determine what is relevant and what the potential harms or outcomes may be. A good example is strata insurance commissions. There is no requirement under the legislation to explain to clients how the commission payment is used by the managing agent. Is it just profit? Is it used to subsidise services? (If so, which ones?) Is it used to subsidise the services across a manager's portfolio? If so, are some schemes receiving a benefit over others in the portfolio?). These types of questions only go to content relevancy. Who determines what content is relevant to a duty-owed person may be complicated and certainly needs consideration.

An assessment would also need to evaluate how the information is conveyed (use of language), how much information is conveyed, whether the information is misleading, and whether the information is easily accessible and well presented.

Even if governments required a more detailed disclosure regime three problems remain:

a) The duty-bound person (the manager) is not absolved – disclosure does not cure the conflict of interest. The underlying duty remains, and the duty-bound person still faces an ethical problem. There is no silver bullet.
b) Disclosure is not consent – the duty-owed person is simply being informed about a conflict of interest situation not agreeing to the practice or relationship. Being told that a wrong-doing will occur or has occurred is very different from approving or agreeing

[50] Office of the Commissioner for Body Corporate and Community Management, Common Ground (Issue 46, 2 July 2024) https://app4.vision6.com.au/em/message/email/view?a=55581&id=1813804&k=VYB-zUGH0X4slQAW3DFPi9GAX6oJRQbWm4KSlhaRVhc.
[51] Minister for Better Regulation and Fair Trading (Ministerial Media Release, 11 February 2025) https://www.nsw.gov.au/ministerial-releases/transparency-at-heart-of-strata-reforms
[52] Omri Ben-Shahar and Carl E. Schneider, 'More Than You Wanted to Know: The Failure of Mandated Disclosure' (Princeton University Press, 2014); Carl E. Schneider and Omri Ben-Shahar, 'The Failure of Mandated Disclosure' (2011) 159(3) *University of Pennsylvania Law Review* 647.

to the wrong-doing. Although informed consent (full disclosure of all material facts) can legally cure a breach of fiduciary duty, it is still ethically and psychologically problematic.

c) There are cognitive impediments that exist for both duty-owed and duty-bound people that makes disclosure (even full and frank disclosure with consent) an ineffective mechanism.

1.8 The cognitive impediments[53]

The psychology of disclosing a conflict of interest – perspective of duty-owed (the owners corporation)

It is assumed that disclosure automatically alerts the duty-owed person to the conflict of interest and in return they can discount the advice or information from the duty-bound person so an optimal decision will be made. Unfortunately, this assumption does not consider how a person mentally processes the biased information. Studies have shown that people have difficulty in judgmental correction, that they fail to discredit or unlearn false and misleading information, there is a correspondence bias, and people suffer from insinuation anxiety.[54]

1.8.1 Difficulty of judgmental correction

For a duty-owed person to evaluate and discount corrupted or biased information, preconditions must be met. The person must be motivated enough to make correct judgements, they must be aware of the potentially distorting influence, and they must understand the direction and magnitude of the influence.[55] These preconditions are rarely met. Estimating or calculating the magnitude of the bias is extremely difficult. That is, it is difficult to determine the effect that the conflict of interest has in any given situation. Although it might be apparent that caution should be taken, there is uncertainty around exactly how much.[56]

1.8.2 Failure of evidentiary discreditation

When people are given clear instructions to discredit or discount information, they still have trouble unlearning false or misleading information.[57] People continue to be influenced by discredited information and over time, false information can become believable.[58]

1.8.3 Lay dispositionism and the representativeness heuristic

The known character or disposition of the duty-bound party plays a role in how the duty-owed person responds to disclosed information. "[P]eople have a tendency to assume that behavioural outcomes are representative of the dispositions and character of the individuals who commit them, underplaying the role that the situation had in determining the behaviour.[59] The disclosure of a conflict of interest by a duty-bound person who is perceived as ethical and upstanding may have little or no impact on the decision being made. Trust in the duty-bound person plays an important role. If the party with the conflict of interest appears candid and honest then disclosure may serve as an assurance of trustworthiness. As a result, biased information may be ignored.

[53] Note: this section of the paper is based on previous work by Nicole Johnston and Karla Johnston See: (n 42).
[54] Cain (n 46)
[55] Ibid.
[56] Ibid.
[57] Ibid.
[58] Ibid.
[59] Ibid 113.

1.8.4 Insinuation anxiety

If the duty-owed person fears that rejection of advice may be interpreted by the duty-bound as an indication of distrust, they may not take steps to question the information or advice. After disclosure of a conflict, refusing a recommendation can be tantamount to insinuating that the adviser is a crook. People often try to maintain harmony and as a result the disclosed relationship or practice is ignored without further enquiry. Studies have shown that conflict of interest disclosures decrease trust but can increase pressure to comply due to insinuation anxiety.[60]

The psychology of disclosing a conflict of interest – the duty-bound (the manager)

At the centre of any conflict of interest is the question – can those owing duties set aside their own self-interest for the benefit of others? Many professionals will argue they have the ability, once confronted with a situation where they may benefit, to act solely in the interests of another. Believing you are an ethical person may not be enough to eliminate acting in a self-interested manner.

1.8.5 Disabling self-interest

History has repeatedly demonstrated that rewards or the anticipation of rewards, specifically money and/or power, are the key determinant variables in behaving ethically or unethically.[61] To determine a course of action, humans engage in a risk/reward calculation, where risk is contemplated from detection through to anticipated punishment, and reward derived from the likelihood of accumulated benefits. Some risks will be evaluated as simply not worth taking because cheating someone could result in a negative self-image and sustained reputational damage. Others will encounter a self-serving bias.[62] This approach occurs when a person makes a (substantial) gain from reaching a certain conclusion. So they unknowingly assimilate evidence that favours that conclusion (undue influence). Even more problematic is the myopic blind spot bias that often follows the discovery and awareness of self-interest exposure. Paradoxically, such exposure makes us feel more confident in our own judgement in seeing self-serving biases in others rather than ourselves.[63]

1.8.6 Strategic licensing and moral licensing

Furthermore, studies have shown that duty-bound people often give more biased advice after disclosing a conflict.[64] Disclosure can compound the problem due to strategic exaggeration and moral licensing. Strategic exaggeration occurs when a person fears a disclosure will lead to the advice or information being discounted so to counteract this, they compensate by further skewing the advice.[65] Moral licensing is a subconscious phenomenon that results in a person worrying less about the consequences of immoral behaviour because of a bolstered self-image. This means they are more likely to act immorally or selfishly.

The use of disclosure as the main mechanism to combat conflicts of interest is at odds with how humans mentally digest such information. Duty-owed people are unable to easily discount conflicted information due to a variety of factors. Furthermore, duty-bound people are unable

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[60] Sunita Sah, George Loewenstein and Daylian Cain, 'Insinuation Anxiety: Concern That Advice Rejection Will Signal Distrust After Conflict of Interest Disclosures' (2018) 45 (7) *Personality and Social Psychology Bulletin* 1099.
[61] Diana C Robertson, Christian Voegtlin and Thomas Maak, 'Business Ethics: The Promise of Neuroscience' (2016) 144(4) Journal of Business Ethics 679.
[62] Jason Dana, 'How psychological research can inform policies for dealing with conflict of interest in medicine' in Marilyn Field and Barnard Lo (eds), Conflict of interest in medical research, education, and practice (National Academies Press, 2009) 358.
[63] Ibid.
[64] Cain (n 46).
[65] Ibid.

to easily act in a manner that does not serve their self-interest. A further compounding factor is that mental processing is both automatic and unconscious. People are unable to make neutral judgements because mental processing makes it difficult.

Part 1 has provided an overview of the types of risky dealings previously reported, why strata is a high-risk conflict of interest industry, how conflicts of interest should be conceptualised, what mitigation and management strategies could be used, and why information disclosure is an ineffective regulatory tool to combat conflicts of interest.

Part 2: Methodology

This study adopted a qualitative research approach employing multiple data collection methods to investigate strata management practices and relationships that give rise to conflicts of interest. The research design utilised methodological triangulation through three complementary techniques: analysis of strata management company websites and agreements; interviews with primarily senior strata managing agents; and participant engagement sessions with strata lot owners. This mixed-method approach was selected to provide comprehensive insights into the complex relationships and practices that give rise to conflicts of interest. This enabled the structural analysis of industry practices and an exploration of stakeholder and lot owner experiences and perspectives.

A qualitative methodology was most appropriate given the exploratory nature of the research questions and the need to examine complex interpersonal and organisational relationships that have received limited empirical attention. The convergent mixed-method design allowed for simultaneous data collection across different sources, facilitating comprehensive triangulation of findings.

2.1 Research activities

2.1.1 Phase 1: Preliminary unstructured interviews with strata management principals and strata lawyers (National)

Unstructured interviews were conducted at the beginning of this research project with six strata professionals who had shown concern regarding conflicted practices and relationships. The purpose of this phase was to identify practices and relationships of concern to ensure they were further investigated.

2.1.2 Phase 2: Review of websites and management agreements (NSW)

First, a systematic review of 153 strata management company websites was conducted to determine the range and types of services provided to owners corporation clients. This analysis served to identify potential areas where conflicts of interest might emerge through dual service provision or relationships.

Second, a comprehensive review of 35 strata management agreements was undertaken to examine disclosure practices. The agreements ranged in execution dates from 2021 to 2025. This activity provided insights into formal contractual arrangements and the extent to which potential conflicts are acknowledged and communicated to owners corporations. The analysis focused on clauses relating to disclosure obligations including third-party relationships that might create conflicts of interest.

This first phase analysis examined organisational practices and relationships without researcher influence, providing an objective baseline for understanding industry standards and practices. This systematic approach identified patterns across different organisations and established contextual background used in subsequent data collection phases.

2.1.3 Phase 3: In-depth Interviews with strata managing agents (NSW)

Semi-structured, in-depth interviews were conducted with 20 strata managing agents, who were principals or senior practitioners. Interview duration ranged from 53 to 92 minutes with over 20 hours recorded. This sampling strategy ensured access to individuals with comprehensive knowledge of industry practices and decision-making authority regarding conflict-of-interest situations.

The interview methodology was designed to empirically examine three key research domains: (1) the relationships and practices that give rise to conflicts of interest within strata management; (2) the actions undertaken by managers when confronted with conflicted interest situations; and (3) the perceived impacts these relationships and practices have on strata property owners.

Purposive sampling was used to select participants with diverse experiences across different types of strata properties, management company sizes (125 to 50,000 lots), and geographic regions (Sydney metropolitan areas and regional NSW). This ensured maximum variation in perspectives while maintaining focus on practitioners with direct experience managing conflict of interest situations.

The semi-structured interview method enabled exploration of sensitive topics related to professional ethics and business practices that might not be documented in formal materials. This allowed for the emergence of unexpected themes while ensuring consistent coverage of core research areas across all participants.

2.1.4 Phase 4: Participant engagement sessions with strata lot owners (NSW)

Two structured online sessions were conducted with 16 strata lot owners to assess their knowledge of common conflict of interest situations with an emphasis on insurance commission processes. These sessions employed a participant observation approach where strata lot owners were presented with different components of the insurance commission process and their responses were systematically observed and recorded.

This method served a dual purpose: first, to empirically assess the level of awareness regarding potentially conflicted practices; and second, to observe the reactions and decision-making processes of strata lot owners when they were presented with information about industry practices. The sessions were designed to minimise researcher influence while capturing authentic responses to scenarios representing real-world situations.

The participant engagement approach was selected over more traditional interview methods so when participants were confronted with industry practices their knowledge levels and decision-making processes could be captured accurately. This method created scenarios that mimicked real-world situations and providing insights into the practical implications of current disclosure practices and lot owner understanding.

2.2 Integration and triangulation

The three methods were designed to work complementarily, with each addressing different aspects of the research questions while enabling comprehensive triangulation of findings.

This methodological approach examined conflicts of interest from multiple perspectives: formal organisational structures (Phase 2), practitioner experiences and decision-making (Phase 1 and 3), and strata lot owner impact assessment (Phase 4). The integration of methods allowed for cross-validation of findings, with consistent themes emerging across different data sources lending credibility to conclusions.

2.3 Data collection and analysis procedures

Data collection occurred over eight months, with Phase 1 conducted first to establish contextual understanding, followed by concurrent interview and participant engagement phases. All interviews were audio/video-recorded (using zoom software) with participant consent and transcribed for analysis. Phase 3 engagement sessions were video-recorded to capture both verbal and behavioural responses.

Thematic analysis was employed across all data sources, with initial coding conducted independently before cross-method pattern identification and theme development. The analytical approach followed established procedures for qualitative data analysis, including systematic coding, theme identification, and iterative refinement of interpretive frameworks.

2.4 Research findings

2.4.1 Phase 1: Preliminary unstructured interviews with strata management principals and strata lawyers (National)

The purpose of these interviews was to understand practices and relationships that might lead to a conflict of interest. As highlighted in the methodology section, the interviewees raised concerns about what they considered unethical practices

Table 1 summarises the practices and relationships the interviewees believed interfered with a strata manager's ability to uphold their best interest duties. These interviewees had experienced or witnessed practices and relationships they considered a breach of a strata manager's fiduciary duty, clear conflict of interest, or unethical. They identified some areas as widespread practices (insurance commissions, developer consulting work, staff remuneration commissions, and training). They also identified areas pertinent to larger strata management firms (affiliated and associated entities, event sponsorship, and supplier/service provider kickbacks).

There were practices and relationships identified by individuals that were unknown to others in the group. For example: suppliers and service providers being invited to become education sponsors for management firms. Sponsorship brochures showed various levels of cost commitment, but all ranged in the thousands of dollars. A committee member that provided this example said the pressure placed on the committee to use the management firm's education sponsor was tantamount to bullying.

Overwhelmingly, interviewees wanted these practices and relationships eradicated from the industry. The general sentiment was that governments needed to consider these practices and relationships when formulating policy and undertaking any law reform.

Table 1: Overview of practices and relationships raised as potential conflicts of interest in Phase 1 of research project

Conflict of interest topics	Practices / relationships
Commissions – insurance, energy	Strata manager receives a commission from insurer/broker based on insurance premium or from energy broker.
Developer consulting work – front end structuring	Strata manager undertakes pre-registration consulting work for scheme developer for low or no fee in exchange for strata management agreement, insurance commission, certificate fees or other benefits (trips).
Service provider / supplier referrals	Strata manager receives/demands a fee or other benefit from supplier or service provider for referring company to owners corporation clients.

Affiliated and associated entities	Strata manager (entity, directors, employees) has a legal or familial relationship with another entity (or its members) that provides services to strata manager's owners corporation clients.
Staff remuneration schemes based on additional services	Strata managers (staff) remuneration tied to owners corporation additional services charges – incentive/bonus.
Training	Strata manager receives training from supplier or service provider for free or non-commercial rate in exchange for preferred supplier status.
Event sponsorship	Strata manager receives payment from supplier or service provider for hosting or paying for events – e.g. party and in exchange supplier receives work from owners corporation clients.
Software / bank integration	Strata manager only holds accounts with one banking institution – as accounting software is integrated with that institution. In exchange the strata manager receives some benefit including reduced software fees.
Gifts	Strata manager receives a gift from supplier or service provider for referring owners corporation clients or as an incentive to do so.

2.4.2 Phase 2: Review of websites and management agreements[66]

Of the 153 websites reviewed, 15 were related or subsidiaries of larger strata management firms. Aside from general strata management services that all companies provided, 47% (n=72) of websites promoted developer structuring and consulting services, 15% (n=23) provided building management or facility management services (either directly or through associated entities), 12% (n=18) offered real estate (sales, property management) or other consulting type services, and 4% (n=5) highlighted education partnership arrangements.

Of the 35 strata management agreements reviewed, eight general categories of disclosure were identified:

- Insurance
- Associated/affiliated entities
- Energy
- Finance and banking
- General compliance (capital works plans, workplace health and safety reports, valuations etc)
- Training and education
- Developer consulting
- Gifts

Insurance - The majority 91% (n=32) disclosed that a rebate, commission or fee was paid by an insurer or broking firm. Three remaining agreements did not disclose an insurance commission. One agreement stipulated that no commissions or inducements of any kind (including insurance) were received. One agreement had no disclosures at all, and the last of the three stated no insurance commissions were received but disclosed a business relationship with an insurance broker. In terms of how the commission was described, the majority stated the name of the entity (insurer or broker) and 'up to' a stated percentage of the base premium. Although the percentage commission ranged from 9 to 25%, most stated the commission paid was up to 20% of the base premium. Regularly, and at times as an

[66] Note: It is acknowledged that substantial reforms occurred in NSW in 2025 relating to disclosures and that more substantive disclosures may have occurred at annual general meetings. The purpose of this analysis is not to investigate disclosure compliance but rather flag practices and relationships that may give rise to conflicts of interest.

alternative, a percentage of the broker fee as a commission was stated. For example, ‘or 50% of the broker fee’.

Seven agreements named only one preferred broking firm, 15 named between two and five firms, four named more than five firms, three stated ‘any broker we appoint’, one stated ‘for the placement of insurance’ with no reference to any insurer or broker and two had no information regarding brokers.

It was observed that several agreements included a statement similar to the following:

> *“Where the owners corporation arranges for placement of the insurance cover or engages a third party i.e. an insurance broker, the agent is indemnified by the owners corporation to the extent of liability contributed by an act, omission or negligence on behalf of the owners corporation or third party in placing the insurance cover.”*
>
> *“To assist with the Strata Manager's performance of its obligations under [clause stated] of this Agreement, the Strata Manager will use the services of [named associated broker], unless the Owners Corporation directs the Strata Manager to use the services of a nominated insurance broker to provide insurance services to the Owners Corporation.”*

These clauses were highlighted because previous research had raised questions about insurance brokers. In particular, whether brokers were appointed by owners corporations for insurance-related services or appointed by strata managers to fulfill their obligations to obtain insurance quotes under the *Strata Management Act 2015*.

Associated / affiliated entities - The next most prominent disclosure made related to associated or affiliated entities with 46% (n=16) disclosing a relationship (either directly (subsidiary of management company) or indirectly (familial relationship connection, director/shareholding in associated company). The types of services provided by these entities ranged from maintenance, plumbing, insurance broking, remedial work, legal, valuation, insurance, property, tax compliance, fire protection, and energy brokering. How the relationship was described varied across the sample. ‘Subsidiary’, ‘related party’, ‘related bodies’, ‘agent was not independent and had a commercial arrangement’, ‘associated company’, ‘relationship’ are the terms/phrasing used. It was rare that more detailed information regarding the relationship was provided. Many disclosures in this category appeared in smaller font than the rest of the management contract. Many of the agreements stated that although the ‘*related entity*’ was recommended, the client owners corporation had choice in terms of engagement. Only one company stated that the owners corporation client received a considerable discount if the ‘*related entity*’ was engaged for those services. Generally, the agreements stated that any fees generated by the ‘*related party’* were retained by it and not the managing agent.

Energy – Nearly 26% (n=9) of the agreements reviewed had a commission or fee arrangement with an energy broker. Typically, the disclosure provided the name of the broker company and the percentage of the commission based on the commission that the broker received (ranging from 30 to 35%). None of the agreements provided an indication of the dollar amount received or the percentage or dollar amount received by the broker. Some agreements stated the commission percentage in terms of energy usage, for example, less than 1% of the total energy usage cost or up to 3% of energy expenses.

Training and education – Only 20% (n=7) of agreements disclosed information relating to education and training. Often the description stated the names of various companies (law firms, suppliers, and other service providers) and that the strata management company received the benefit of training. Some agreements provided an explanation as to why the training was important and the benefits that flowed to owners corporation clients.

Finance and banking – A small percentage (8%) of agreements disclosed a fee or commission relating to banking and finance. The majority related to strata loans. The description used varied from a percentage (e.g. up to 1%) with no additional information, to a percentage (0.40%) of the draw loan balance for the life of any loan. One agreement simply stated a percentage (0.25%) from a known banking institution with no further information.

General compliance – Only 14% of agreements disclosed that a commission or fee had been received by a supplier of compliance type services (e.g. capital works plans, valuations, and workplace health and safety reports etc). Several agreements either just stated the company name (with no further details of the fee, commission or arrangement), or that they may receive a benefit from suppliers where they had negotiated a concession on products and services on behalf of multiple clients. Others included the percentage received based on the cost of the report (e.g. 7.5% to 15%).

Developer consulting – Only one agreement disclosed developer consulting work. The description stated that advice had been given pursuant to the Act for creating owners corporation records and holding the first annual general meeting. No information was provided in relation to any benefits received.

Gifts – Four agreements referred to gifts. One agreement stated that 'no gifts or hospitality of a value greater than $60 would be accepted from any third-party providers to the scheme', another stated that the gift registry could be inspected on request and the others stated that they benefited from Christmas gifts.

2.4.3 Phase 3: In-depth interviews with strata managing agents (NSW)

2.4.3.1 Categories

The interviewees participating in this research phase fell into four categories based on their ethical positioning.

Category 1: Traditional commission-dependent operators

Six of the participants could be best described as commission-dependent operators, relying heavily on insurance commissions as a source of revenue. These operators disclosed that insurance commissions made up 15-25% of their revenue and a substantial portion of their profit. The interviewees acknowledged the industry problems associated with insurance commissions and other practices. However, they felt that the current disclosure requirements provided enough transparency for clients and that a ban of this form of commission would lead to, as one interviewee put it, chaos. The following quote captures what many in this category thought:

> *"If we're talking about insurance commissions generally. I think obviously it's a well-trodden practice in terms of strata but also other industries... as long as it's open, it's disclosed and people are aware of it. And they're [clients] going into it with eyes wide open and it's a commercial discussion. They understand what the money is for and how it's being used, I guess, in our practice and with the strata industry generally, it's being used to subsidise base costs. Where I've seen things that I don't believe are absolutely good or kosher is where you have insurance companies or subsidiary-brokerage firms coming to strata management companies to get security over their insurance work."*

Category 2: Reform-oriented operators

Six of the participants could be best described as reform-oriented operators. These operators had either eliminated commissions and other conflicted remuneration or had never taken commissions. Many interviewees in this category had started their own business running on a

platform with no conflicted remuneration after working in other strata firms. As illustrated by this interviewee:

> *“One of the main reasons why I had started my company was because of all these dubious relationships and happenings that were going on in the industry.”*

These interviewees stated that their base management fees were higher than most in the industry but had no issues in explaining the pricing model to clients or retaining clients. They felt they now had a competitive market advantage due to their ethical stance on conflicts of interest.

Category 3: Whistleblowers/critics

Three of the participants could be aptly described as industry whistle-blowers. These operators provided details of practices and relationships that at the very least would be considered unethical but arguably are a breach of managers’ legal duties. These participants named companies and specific practices that may not be commonly discussed.

One interviewee explained how a previous employer was focused on monetising every transaction with little care for the duties they held. They explained that staff were encouraged and rewarded through remuneration bonus schemes to charge unnecessary fees to owners corporation clients. This interviewee explained that often management companies use their delegated duties to achieve this outcome. The phrase ‘tap and go’ was used to explain the mentality of the management firm.

> *“They [named strata management firm] are trying to monetise every transaction. Your fiduciary responsibilities are to your principal, to the client, but you're also being told that there's incentives here if you point them this way. That's a conflict. That's not right. That's not on. So if you use these trades, if you use this one, if you use this system, you'll be rewarded.”*

Category 4: Transition/conflicted operators

The fourth category of interviewees could be described as the transition/conflicted operators. Most of these interviewees acknowledged problems in the industry but were still engaging in conflicted practices. They appeared to be caught between their own ethical concerns and business viability. They all expressed intention to reform and had made efforts to move away from insurance commissions and developer consulting work but were waiting for legislative reform banning these practices. In their mind, a level playing field was required to ensure that the current practice of undercutting on base management fees is alleviated. Their position was that if insurance commissions and other conflicted remuneration were banned then everyone was simply competing on service delivery.

2.4.3.2 Comparative thematic analysis of interview data

Seven general themes emerged from the interview data analysis. These themes aligned with the questions asked to the interviewees.

Theme 1: Impact of media scrutiny - universal but varied responses

Interviewees were asked about the impact of the 2024 ABC reporting had on their business, their staff and the industry more generally. According to interviewees, there was an immediate reaction from many strata lot owners and significant time was taken to explain the model utilised in the individual businesses.

> *"The next day it started... It took up a lot of my time face-to-face with people."*

Some interviewees explained the emotional distress that the reporting had on staff with accusations of widespread unethical conduct.

> *"It definitely painted the whole industry with the same brush and it didn't feel fair."*

The responses from interviewees when being questioned by strata lot owners appeared to vary depending on operator type. Traditional operators felt a negative initial impact when clients expressed their discomfort about the taking of insurance commissions. Small to medium traditional operators who said they do not participate in other conflicted arrangements aside from the taking of insurance commissions, felt they adequately explained the business model to their clients and in some instances experienced business growth as owners corporation clients moved away from larger firms with integrated service models. Reform-oriented operators were more positive about the media attention and felt the scrutiny validated their ethical approach to strata management. For these operators, their conversations with clients were short lived as they could promote their commission-free model.

One interviewee believed the issues raised in the media would continue and provided some insights about why strata owners and committees may be suspicious of the strata management industry.

> *"I think it [the ABC reporting] heightened suspicion amongst owners and committees around what might be lurking beneath…what it is that they can't see. I think that comes from a legitimate perspective that we do have a privileged position of being both a party that has access to their accounts, can do work for them, and can almost effectively pay themselves based on the management agreements that they've got. And when you throw in the concerns that get raised by the media, it starts to get a real momentum and there becomes that confirmation bias that the client is looking for evidence to justify … it certainly hasn't gone away it tends to rear its head when insurances get renewed."*

The reporting made many reevaluate the practices and relationships in their own businesses. Conversations had begun internally with staff and committees and steps had been taken in terms of provider referrals. Concerns raised regarding a particular company prompted one company to change to a non-affiliated insurance broker.

> *"And we were actually quite happy with the brokers that we were using but from a market perception, it was hurting us. And so we made that choice to say, okay, well, let's again, eliminate the conflict, because disclosures just weren't good enough in this situation. There's been disclosures forever in a day, but the disclosures disclose conflict."*

Theme 2: Insurance commission practices - the central business model dysfunction

Unsurprisingly, the interview discussions predominantly concentrated on insurance commission practices. The discussion focus for each operator type varied. The traditional operators concentrated their points on revenue dependency. The reform-orientated operators focussed on conflicts of interest. The transition operators spoke of the need for change and the processes that they had started to employ to move to a commission-free model.

Profitability was a major concern for the traditional operators. It was evident these operators feared for the viability of their businesses. There was widespread concern regarding the uplift in management fees to ensure profitability. These concerns were more acute for smaller business operators situated in less affluent areas.

> *"If insurance commissions are prohibited, there will be no profit for the business. Insurance makes up 18% and 1/3 profit. We would have to increase fees substantially to make profit."*

"*If the government bans the commissions and therefore no one's subsidising your manager anymore and we've to pay staff and we've got run a business. So therefore we pay more out of our pocket."*

Some viewed the NSW Government's position to ban commissions as an overreaction to a few in the industry engaging in unscrupulous practices. Others appreciated that the "optics regarding insurance commissions does not look good" but these operators believed that a ban of insurance commissions would lead to increased costs for the consumers and that insurance companies would increase their costs in any event.

"You can't change the legislation because of a couple of bad actors. You need to make an example of them. If insurance commissions are banned there's going to be quite a lot of upheaval. I think if we all increase fees by 15% or 20%, we can do that, increase by 15%. The insurance companies who are bound by national legislation may give a cost saving in the first year, but what about year two? So if we're going to change it [insurance commission arrangements], the insurance companies will go - our cost base has changed. Then what happens to the consumers? Will they really end up the same or better? I don't think so. The NSW government can't control the insurance companies."

"*I firmly believe that the costs will go up significantly for the consumers and that insurance companies will be the ones to profit at the expense of everyone."*

The overriding sentiment expressed by the traditional operators was that the current disclosure provisions outlined in the *Strata Schemes Management Act 2015* (NSW) were sufficient and that owners preferred the commission subsidisation model. Many interviewees explained that they had either provided the option to their clients to remove the commission or had discussed the financial impacts that the removal of the insurance commission would have, and most clients preferred the model that retained the existing commission regime. The traditional operators felt that the disclosure regime created a transparent model.

For the reform-orientated operators, duties to their clients were clearly front of mind. Most of these operators never relied on insurance commissions and had built in a higher base fee model from the inception of their businesses. As discussed by several interviewees, remuneration models based on the receipt of insurance commissions created complications, were a clear conflict of interest and were difficult to justify. It was evident to them that the disclosure requirements did not achieve transparency.

"*They're a clear conflict of interest. They're creating complications. We don't need them."*

"I think it's [insurance commissions] a completely unjustifiable impost on owners. It's associated with a whole lot of lies…So there's simply no basis on which, logically, a strata manager should take a commission on anything. And it creates conflicts that you can declare, but that's not enough."

Most of the operators agreed that insurance commissions were used to subsidise management services (including but not exclusively insurance-related services) across their management portfolio. However very few (except the reform-orientated operators) were concerned that the cross-subsidisation model created artificial pricing distortions. That is, owners corporations that pay larger premiums (due to size or other factors that increased premiums) effectively subsidising schemes that pay lower premiums.

As discussed by one reform-orientated operator:

"Those large ones are clearly subsidising the small…because little buildings are being subsidised by their huge insurance commission from the big ones."

These operators denounced the disclosure requirements as effective. They felt that many strata lot owners and committees did not understand the management agreement in detail, were not aware of related broker entities that received a commission and were not aware of how the commission was used by strata management companies or insurance brokers.

> *"We feel like we are unfairly judged because the big players take that commission either through a broker that's a related company or paid direct from the insurer but only disclosed in the AGM notice and not in the financial accounts. I mean, realistically, a lot of the committees don't understand the financial statements. They don't understand the management agreement in detail."*

As highlighted by several interviewees, there were operators that stipulated they don't take a commission but have an affiliation with an insurance brokerage firm. The fees paid to the brokerage firm for insurance-related services were paid by owners corporations through their premiums as a broker fee or as a commission. One traditional operator stated that it was possible and perhaps likely that if insurance commissions were banned that more operators would enter into arrangements with broking firms as an additional revenue source.

The transition operators described the action they had been taking to move away from their reliance on insurance commissions. For many, they were simply waiting for legislative reform that prohibited the taking of insurance commissions. Essentially, these operators were working through remuneration options and having discussions with their clients.

> *"We've basically made the decision, hopefully over the course of the next month, we want to move away from insurance commissions, we want to net all of our clients' policies and have all the brokers competing basically on a broker fee, which I think is a big advantage to the owners corporation because it nets out a lot of the commission which is also payable on the GST and the fire service levy and all these other add-ons."*

The transition operators were conscious that many strata lot owners and committee did not really understand how the insurance commission structure worked and as suggested, often management staff did not understand it either.

> *"We have a few individuals [owners] that really dig deep but no, I think majority [of owners] don't really understand it. And I actually will say that I think even our staff don't necessarily really understand how it all is structured."*

A sub-theme emerged under the broader category of insurance commissions. The engagement and remuneration structures of insurance brokers.

As highlighted in the Phase 2 findings, questions had previously been raised regarding the appropriate appointment of insurance brokers. Interviewee responses varied when asked 'who' and 'how' insurance brokers were appointed. The majority indicated that the appointment of a broker was made under their delegated duty. Therefore, they usually chose the broker unless the owners corporation client was new and had previously engaged a broker.

> *"It's actually in our agency agreement that we've got the delegated authority to make that appointment, so I don't even really discuss it."*

Although the agreement of this interviewee stipulated the engagement of a broker as a delegated duty, most other interviewees seemed to rely on the common description, as outlined in their management agreement, of or similar to – 'arranging insurance cover' as the delegated duty. This allowed them to either engage a broker or circumvent the engagement without an owners corporation resolution.

Very few of the interviewees advised that a motion was put before the owners corporation or its committee to engage a broker.

When asked if a motion that outlined the services provided by the broker and their fees, was put to the owners corporation, all interviewees stated this did not occur.

> *"There is no motion to appoint."*

Some interviewees explained that logistically it was easier to deal with one or a limited number of brokers.

> *"Our preference is to use [named broker company] because it's easy for us to have all of our clients with the same broker rather than dealing with 50 different brokers, that's a bit of a logistical challenge."*

> *"So when we first started out, we went with every broker that was going because I didn't want to be aligned with any and I found out that there were different qualities of broker out there. But it's not exclusive. If people want to use their own, they want to place their insurance direct, they can. And if they want to use their own broker, they could, not that anybody ever has."*

There was a prevailing view that due to the three-quote rule (*Strata Management Act 2015* s.166) it was necessary to engage the services of an insurance broker. Although some interviewees did not understand it was the strata manager's obligation to obtain the quotes not the owners corporation.

> *"We notify them [owners corporation clients] that under the legislation, they need three quotes, therefore we have to get a broker."*

This renewed understanding of who was responsible for obtaining the quotes, created understandable confusion about whether the insurance broker worked for the strata manager or the owners corporation.

There is a separation in terms of service delivery and the responsible party. It is the responsibility of the strata manager to obtain the quotes and it is the responsibility of the owners corporation as the insured to place the required insurances (although often delegated). Although many interviewees supported the provision to obtain three quotes, those that understood the responsibility thought that amendments were required to place the onus on the owners corporation.

> *"I actually would prefer the provision to state that three quotes must be obtained by the owners corporation."*

> *"Think it is a good thing. Obligation should be on the owners corporation though."*

One interviewee explained that the three-quote rule was necessary due to the variations in premiums.

> *"I think it's absolutely crucial [to have the three-quote rule]. Having worked on the insurance for the last 10 years, premiums still surprise me. I find the range between the different insurers huge and very unpredictable as to who will come in cheaper. I am still shocked that you could have a 200% variance in quotes on the exact same terms.*

Although this interviewee supported the rule they believed the variations related to unscrupulous practices by associated entities (insurers, brokers and strata managers).

> *There are strata managing conglomerates that have vested interests and shareholdings in brokers, they're getting kickbacks from the broker, they're getting kickbacks from the insurance company or whatever you want to call it, it is not transparent and even with the changes in the legislation, it's still not. So even getting three quotes, you're still going through the broker that's in house or a fully owned subsidiary or whatever, in any other industry, that would be unacceptable.*

For most interviewees, particularly the reform-orientated operators, it was agreed a ban on commissions should extend to both strata managers and insurance brokers. A 'fee for service' model was preferred, with interviewees mentioning that a select few insurance brokers were offering this option. One interviewee explained that although a' fee for service' model was preferred, they appreciated there was more instability in terms of brokers' work (particularly around claims) that may require a commission approach to remain viable.

> *"They have to take the risk on some schemes having lots and lots of claims and others having no claims. And they don't know where they're going to make their money and where they're going lose money. And that's their business. I'd have been happy to work with a broker that took a nominal fee for the placement of the insurance and then charged by the hour for the claims management but that's just how they tend to work. But I think if it's transparent and able to be compared with other brokers and what they charge, then a percentage of the base premium is probably reasonable because it's probably going to be more work with a bigger scheme than a smaller one."*

Theme 3: Schedule B billing – staff incentivisation

It is common practice that management staff are remunerated by way of a base salary plus superannuation plus a commission. The commission structure is based on the billing of Schedule B fees. Schedule B fees are usually fees that are generated from additional services (outside the agreed services and general disbursements). Common employment advertisements reviewed[67] indicated the widespread use of this remuneration model. Examples include:

- Up to $140k base + super + approx. $40k in Schedule Bs
- 50% of Schedule Bs and new business comms
- $110k + super + meeting fees + bonuses
- Base + comms/bonuses
- Incentives and commission options to boost earnings
- Solid six figure salary package plus Schedule Bs
- We offer Schedule Bs
- $100 to $110k plus earning bonuses through additional Schedule B charges
- $130k + super + Schedule Bs
- $80k to $120K per annum plus Schedule Bs

Questions asked about the use of Schedule Bs as part of the staff remuneration model elicited the most diverse responses. Traditional operators were either defensive and chose not to answer or explained the necessity of Schedule Bs. For example,

> *"Managers attend after hour meetings and there's only so much salary you can give… then there are unknown variables that the customer creates."*

> *"It rewards the people that work hard."*

One interviewee explained that accountability checks were imbedded in their business to ensure that owners corporation clients were not overcharged.

> *"They're entered into a CRM system. They are cross-checked against - if it's a meeting, what time they attended the meetings, it's cross-checked against correspondence and the time brackets, etc so on. As a business, we audit, you know, a random spot check and go, hey, come*

[67] Seek advertisements were reviewed on 19 September 2025. Search terms used were 'strata manager' and 'New South Wales'.

on, let's take a look. So that is an obligation of the licensee of a business or a director of a business."

The reform-oriented operators and whistleblowers found the practice problematic and suggested that businesses just pay their staff a good wage.

> *"Other businesses have anywhere between 30 to 50 percent split commission of schedule fees. I do find that there is a conflict when you are providing commission to your staff members just to charge clients."*

Concerns were raised about the potential to overcharge clients.

> *"I think incentives matter but there can be unintended consequences like client overcharging."*

Interviewees recounted the emphasis placed on charging Schedule B fees by previous employers and the perverse culture that resulted.

> *"Other companies I have worked at encourage staff members to charge schedule fees. Some of the companies, especially the corporations I've worked at, we had KPIs. We actually had to charge a minimum of $10,000 for the schedule fees a month to even see a cent of our schedule fees. So, look, every company has their own business model. I'm not going to point the finger at how people run their business, but I don't think that's particularly fair, especially if I was a consumer. That's not the way I would like to be treated."*

> *" At [company named] a massive lump of your salary was the Schedule B fees. The more you charge the client, the more you monopolise their time... the longer the meetings went, the more money you get"*

The transition operators felt caught in a trap where this type of remuneration model was common practice making it difficult to compete for staff. These operators accepted the arrangement when it was limited to compensating managers for attending evening meetings. It was their view that the practice started when managers worked all day and then attended meetings that extended late into the evening. They felt that this service should be compensated by owners corporation clients. The concern for many of these operators was managers were now being rewarded through this remuneration scheme for all types of services including remedial work. One interviewee explained the origins, how it had changed and how it had become an accepted practice that was difficult to escape:

> *"And it's just like insurance commission, it has just been accepted. And that was how you remunerated your managers for their overtime. I think that made perfect sense. It was a revenue stream for us, and people were happy to be compensated for doing that work, because they'd to drive to the client, you know, have the meeting, then drive home, and sometimes you wouldn't get home to nine o'clock. So that just became a thing. Everyone did it. The difference is some people will pay Schedule B percentages to their staff for other extracurricular work. This is defects, could be remedial work and all that kind of stuff. So there's this real period of unrest where managers can go down the road to work. Manager down the road is going to pay me 50% of Schedule B's and it's just become commonplace that you know everyone's charging their Schedule B's and pretty much everyone's paying their managers for it."*

Theme 4: Developer relationships – competing obligations

Although a significant portion of business websites stipulate that they engage in developer consulting work, very few of those interviewed undertook this type of work in any significant way. Surprisingly, many of the traditional operators also opposed developer consulting arrangements, highlighting a distinction between conflicted interests and what is and is not acceptable. For the interviewees that do not provide these types of services, their position was clear that it was a conflict of interest and that you cannot serve two masters.

"The relationship is a poisonous chalice – there is pressure to low ball levies."

"When we first started the business, we actually wanted to advocate ourselves as not having any alignment with developers to show no conflicts of interest. We wanted to be absolutely clear as the advocate for the owners corporation."

"I see our role as working for the schemes and not for the developers, and I don't think you can effectively do both."

Some interviewees saw the developer consulting market as a great opportunity to increase business revenue. These operators had not considered the risks associated from a conflict-of-interest perspective.

"We're trying to crack into that little market [developer consulting] because that would be wonderful for us."

Those interviewees that provided these services on a regular basis explained that the model is largely based on no direct fees (that is, the developers were not charged directly for the pre-registration work). However, managers received an initial management agreement (until the first AGM), insurance commission and fees generated from the production of section 184 certificates. As explained, often the manager would be reappointed at the first AGM for a three-year agreement.

No, we don't get paid directly. We get, for a new project, there's quite a large windfall of cash that comes on registration of the strata plan. So for example, for a 200-lot strata scheme that's completely sold when it finishes, we have to produce section 184 certificates for every lot, provided it's all sold, so our money comes from that, it would be 200 times the statutory fee, which is currently I think $118.80, so it's like 25 grand… so the developer pays us that. Use to be insurance commission as well, but we're obviously moving away from that."

"Rather than charge them a fee straight up, what we would do as again a commercial agreement would be that, look, realistically, setting the thing up is we're going to get the property in the long run, we'll set this thing up, it's not that much work involved in it, we would charge the prescribed fee for the 184…

The whistleblowers highlighted some of the unsavoury practices that occurred in the industry and the benefits that flowed from development companies including paid overseas trips:

"The big thing for me always is the developer-strata manager relationship. I think that it hurts owners more than anyone talks about. I'm surprised nobody's been sued, to be honest, and it starts off with managers working for developers for nothing, sometimes for years in advance. I'm aware that there are companies that literally have boys' weekends away overseas, like we're talking like lavish, ridiculous. It is everything you imagine a junket being and they're doing it. I know people that have employed pretty women for the sole purpose of giggling and flirting with them, because they're nearly always men in development."

The impacts these types of arrangements had on owners corporation clients were highlighted by some interviewees. These impacts included: low balling of levies (developer pressuring managers to keep initial budgets low to promote sales); building defect mismanagement (including developers pressuring managers to use specific contractors for rectification work); and promoting a structure that gives developers control over the scheme or enables ongoing and additional revenue streams for the developer. As explained, these advices are generally disadvantageous to owners corporations.

"And the other thing the managers do that nobody talks about, and this really kills me as well, and I've seen (previous boss) do it, is they'll go through the bylaws and they'll go through the management statement before they're registered and give the developer tips to keep control. Make sure you've got exclusive signage rights on your commercial lots or make sure there's no

element that you need consent to do whatever on your lots and make sure you have a leasing bylaw that says you have exclusive leasing rights because these developers always have some sort of building management slash rental business on the side as well."

"The pressure to create a budget that suits their purpose and not the actual landscape of what that plan is going to look like is stupid. You can't do your job. That will serve the future owners corporation and win the business in the favour of the development. Those two things again are a massive conflict."

As highlighted in the Phase 2 findings, only one management agreement had disclosed developer relationships in their agency agreement. When asked about this disclosure requirement, interviewees advised there was confusion in the industry regarding this disclosure requirement.

"So it is [a requirement to disclose], but what they say is they don't have a relationship with the developer because they don't pay anything. There's no money exchange because they're doing all this work for free. They claim there is no relationship."

Theme 5: Vertical integration and affiliated entities - scale and sophistication variations

For most interviewees, their business model did not include any associated or affiliated entities. Most saw this model being adopted by the big strata management companies in metropolitan areas.

Some of the traditional operators, viewed the model as acceptable if disclosures were made. They rationalised that in other countries or business environments, integrated business models were standard and worked well. One interviewee explained how the market had changed overtime from a reliance on referral fees (kickbacks) from external suppliers and service providers to larger firms seeing better value in integrated business models. Interestingly, several interviewees believed that the legislated disclosure requirements had effectively facilitated the rise and continuation of integrated business models.

"…we want to own the debt collection company or part of, we want to own the cleaning company, fire company, the electric company, plumbing company. And by the way, you know, we'll just disclose it. And I think then the moral question does come up. Are they really the best person for the job? So I think this whole thing about disclosures is what sort of changed the game. And I think everyone's thought that there was a loophole. Yeah, that's what's changed more, I think the involvement with people in other companies is opposed to backhanders."

"I think that's the biggest thing with the insurance is these joint venture agreements, which 100% have been created for the sole purpose of managers getting around their disclosure agreements and requirements. And my only fear with removing insurance commissions is there will just be other ways. There will be more strata managers owning insurance broking companies."

One interviewee explained how the insurance broker arrangement works and why managers had decided to adopt the model. There was a consistent suggestion that if insurance commissions were banned then more of these types of arrangements would be utilised to maintain a revenue source.

"A mutual deed between the entities, you effectively get a shareholding in a business or a brokerage firm. And it's always been sold on the basis that when insurance commissions go, then your revenue line, your stream of income will be protected, you'll have a competitive advantage. That's kind of how it's been sold. And so again, you know, I completely understand why some of the strata companies have taken the deal. It's very hard in this day and age to be competitive in this market, particularly where large companies, they've integrated service models and I guess that's the nature of the economy and you see that across many different

industries. That's all well and good, provided it's disclosed, consumers know truly what it is that they're getting into. I don't necessarily have a problem with that, but where it's not disclosed and where people are being misled or they're saying one thing and actually doing another, to me that doesn't sit right."

The majority of interviewees largely rejected this business practice and could see, especially if the strata management firm had full delegated authority, how easily owners corporation clients could be overcharged or not receive the best advice about a service.

"So it's a valid business model saying, we know you're [lot owners] busy…We're professional strata managers. We take care of everything for you, which is a recipe for temptation. It's a recipe for inflated costs without the customer's knowledge."

Most interviewees were very clear about how they viewed the role of a strata manager and adopted a traditional view, preferring arm's length relationships.

The one arrangement that elicited the most impassioned reactions related to affiliations with insurance brokers. Many of the interviewees were frustrated by the rise of strata manager/broker associations. There was clear frustration with strata managers that promoted a non-insurance commission position but had familial, directorial or shareholding arrangement with insurance brokers. Further annoyance was sparked by managers that do not disclose these types of relationships under the guise that the strata management company is not receiving a benefit.

"Forget about the issue about transparency and people going around and saying, Oh, we don't accept commissions, but we've got a shareholding in the company that creates profit and therefore it's not really commissions."

One departure from a pure revenue seeking position came from interviewees in regional areas. Due to limited local suppliers and service providers, strata managers in these areas often relied on familial or associated business relationships out of necessity. They explained that some Sydney-based suppliers or service providers would come to regional areas, but it was more financially advantageous for schemes only when a large proportion of their portfolio requires the delivery of those particular services. Most of these services related to activities where an inspection of the property was required.

"We give them that option [to use other suppliers or service providers] and they go, well, who else is there? We say, well, locally, we don't have anyone. So we're going to have to call them out of area."

One interviewee explained that the husband of one of their employed strata managers often did building work for clients.

"We disclose it but it is not a big deal because the [strata management] company is not receiving a benefit."

Theme 6: Supplier / service provider - the questionable referrals

Although the Phase 2 research findings indicated there were suppliers and service providers engaged in a referral fee arrangement with strata management companies, most of the interviewees advised that such approaches were infrequent except from energy brokers.

"It seems to be like a big thing now. But for me, it was a big thing 10, 15 years ago. You know, I saw it from plumbers and even like, lift companies, not big ones, independent ones would come. I think it's not as prevalent as perhaps the market suggests."

"I've had a few [suppliers / service providers] want us to do things that are a bit, more referral-based, and some of them, you know, will say, look, come to us with your last quote, we'll always beat it, and things like that, just other unethical practices that we just don't get involved in."

The majority of interviewees that used an energy broker chose not to receive any financial benefit when offered. The prevailing view being that brokers alleviated time-consuming interactions with energy companies that were a constant source of frustration. Interviewees shared the view that energy brokers provided an essential service assisting with the management of their portfolios. Interviewees accepted that brokers received a commission but felt it was reasonable because their clients benefited financially.

I don't think there's anyone particularly that reaches out and does that stuff. I mean, energy services do, in saying that, they're making a profit from it or they're making some money from it, but they're doing it for the good of the people.

Many interviewees explained that these arrangements were often presented by companies new to the strata industry. However, one interviewee believed that referral fees were offered by suppliers and service providers that sponsored the Strata Community Association (SCA).

"What I am finding is that generally, if you are a member of the SCA, you will get approached more than others, because in those events that they have the suppliers that are offering these arrangements and commission structures are SCA sponsors."

The engagement of auditors was another relationship discussed in the interview phase. Most interviewees regularly used the same auditor across their portfolio but explained that owners corporation clients could choose their own. The majority of interviewees weren't concerned with this relationship and didn't see the potential conflict of interest. The overarching position being they were transparent and clients could review financial statements through various portals to ensure compliance. However, several interviewees raised concerns about the affiliation with auditors.

"I would say that strata managers do have a little bit of influence on auditors, because auditors, if they find something wrong, they'll come back to the strata manager and say, look, before we publish the audit, these are the things that can you explain? Can you explain if something doesn't look right? That's really not what it is. If there's worries, who's the customer? The customer is the owners corporation, so that question really should go to the owners corporation, and it doesn't."

One interviewee had an owners corporation client that requested a forensic audit. This was because concerns were raised about the mismanagement of funds from previous management companies. Auditors were told by previous managers that they would not use the auditor's services across their other portfolios unless they retracted their involvement in the forensic audit.

"One of the things that I have noticed is that …sometimes that [previous] strata manager will place a phone call to that auditor and say if you continue with your services, we'll no longer use you across our portfolios. And so we've had instances of when those auditors would retract their involvement from the engagement. Everyone's got conflicts of interest and you know, it's crazy because the industry is too close for comfort."

Interviewees were also asked about practices and relationships with banking institutions. Interviewees explained that their client funds were usually held by one banking institution. Clients were generally unable to choose where their administrative funds were held. Some interviewees explained that capital works funds may be held by another institution that provided a better interest rate. Only one interviewee advised that they had an arrangement

with a banking institution that provided exceptional interest rates but didn't allow for strata software integration.

> *"The only reason we do that [continue with named bank] is we get an exceptional rate on the at-call cash. And for many of our strata plans, they actually earn more money and interest from the at-call cash then what they're paying us in management fees."*

Software integration was a determining factor for banking choice. Some interviewees raised concerns about clients not receiving interest, others assumed that software providers were receiving some benefit. There was a general acknowledgement that good, integrated software was necessary for the efficient running of their business.

> *"Sometimes you get to an outcome that's not a bad outcome, but the path to it is murky and questionable and sounds bad."*

> *"I imagine that they [software company] get some type of remuneration from the [named banking institution]. We disclose that we get a cost reduction in software, a software subsidy… So I guess that's the value proposition to us in that well they [software company] can do it cheaper because they've got some side arrangement that doesn't impact us or our clients, so it's like, okay, so that's how they have funded their business, it doesn't impact me and the clients, but it is still a benefit for my business."*

Theme 7: Supplier/service provider training/sponsorship – the pressure to engage

Many interviewees explained that the market had changed in terms of supplier/service provider-led training. As discussed, suppliers and service providers had previously provided training services for free but now it was something that management companies had to pay for. Interviewees explained what the practice had been:

> *"We used to get holidays, essentially provided by those lawyers, engineers, other relevant party suppliers, under the guise of, this is the training of a trade or whatever…"*

An interviewee agreed that things had changed and thought the disclosure requirements were a step too far.

> *"We used to get a freebie from a lawyer to come and teach us about the legislation changes and blah, blah… they did it for nothing. And on the basis that they probably gave us a bit of free legal advice about challenges we're facing and now like we've got to pay for it. I don't think that's right. I think that's good business."*

Others recognised the conflict of interest and rejected supplier/service provider led training.

> *"We don't have anybody coming and doing training and we don't accept gifts. We just don't. You probably could and disclose, and I think you can do that without a conflict, but it's more trouble than it's worth."*

Some interviewees said that after training services were provided there was often a clear expectation that the service provider would become the preferred supplier. However, in other circumstances the arrangement was only implied resulting in stand over tactics such as constant phone calls.

> *"You get someone from [named law firm] calling and saying, we haven't heard from you for a little while. We want to make sure everybody had the welfare check. So it's implied. It is never overt."*

None of the interviewees participated in inhouse events sponsored by suppliers/service providers. Although many had heard of such arrangements in the industry.

"I've heard stories about golfing holidays away and all sorts of things… that's getting around the referral fee. Like, we haven't given you money. We've sponsored this event or we've taken your team away to play golf for the weekend"

2.4.4 Phase 4: Participant engagement sessions with strata lot owners (NSW)

Five themes were identified in the participant engagement sessions: insurance commissions and transparency; trust erosion and agency conflicts; power dynamics and market failures; affiliated entities and pressure tactics; and financial impacts on vulnerable schemes.

1. Insurance commission structure and transparency

The participants understood that it was common practice for strata managers to receive an insurance commission. Many explained that they had attempted to engage in discussions to remove the insurance commission however only a few were successful. Overall knowledge was lacking about taxation implications, services and portfolio cross-subsidisation, and broker arrangements. Universally, participants were not in favour of a remuneration model that included insurance commissions. They felt a 'fee for service' model was more appropriate and aligned with good business practice. As participants stated:

"I would be much happier paying a fee for a service rather than, you know, a bit of a palm greasing here and there. You've done a job for me. That's fine. I'll pay you for the job you did."

"I think you should be able to negotiate a management fee that covers what they actually do."

It was evident that participants preferred a model that was straightforward and transparent. - a basic model where the owners corporation agreed to services and paid a fee directly for that service. There was consistent frustration about hidden commission structures, managers claiming they don't receive commissions when affiliated brokers do, the lack of disclosure about how commission money is used, and the disconnect between disclosure and genuine transparency.

When it was put to owners that the response from the strata management industry was often that owners don't want to pay and prefer the commission structure, the response from one participant was succinct and clear:

"Rubbish"

Overwhelmingly, participants felt that transparency was lacking. One participant explained that their strata manager had attempted to downplay they received a commission, calling it a fee, even though it was an insurance commission.

"We've had bad experiences with that, mainly a lack of transparency and not understanding it was there and even denial that it was there and they called it a fee, but it wasn't. It was actually a commission. So there was deception involved in that."

Others felt that strata managers routinely used their pricing model (low per lot fee) to appeal to owners who were more cost conscious, the diversion aimed at moving conversations away from questions relating to the insurance commission processes. One participant felt their manager was trying to hide the fee structure to bring down the overall management fee number.

Commissions being linked to premiums was a matter of concern. Participants were aware that the higher the premium, the more money the strata manager was making. For some, this was at the heart of the issue. This concern was certainly more apparent for participants that had seen a large rise in premiums due to building defects in their building.

"The fact that the commissions are linked to the actual premium is more of the problem."

The distrust of the strata management industry was palpable after discussions about the standard insurance commission process. Participants were provided with a detailed overview of how taxes were applied, broker/manager arrangements, and how commissions commonly subsidise both individual scheme services (insurance and others) and subsidise services across a manager and brokers portfolio. This was new information and had never been discussed with any of them. They were shocked that some schemes were effectively paying for other schemes.

> *"They're saying they're being upfront. But, yeah, as pointed out now, when you drill down, that's a load of fill in the blank, you know, BS, quite simply."*

This issue of portfolio cross-subsidisation was more acutely felt by participants dealing with complex defect matters. These participants felt they were unfairly embroiled in a remuneration model that was significantly disadvantageous at a time where they were under enormous financial constraint.

> *"It's not just bigger schemes that are paying bigger premiums. It's all the schemes that have got major works issues that are subsidising. And I can tell you from the one that we've got major works going on, our insurance premium has changed. We've trebled in two years. Trebled. And so, it's not just bigger schemes, it's schemes that have got major issues that are subsidising everyone else's. I think it's just a win-win for the strata managers and the insurance companies. They just freaking bandits and we pay."*

Most of the participants were experienced professionals or came from a business background and struggled to understand how the industry differs so much from other industries.

> *"Of all the industries that I've worked in there isn't an industry as much as a dumpster fire as strata. And part of the reason why that's the case, I think, is that it's just so convoluted and so much stuff is happening that is not transparent. The root cause of a lot of the friction is just the way the industry is run, and potentially just the lack of regulation and governance."*

2. Trust erosion and agency conflicts

There was strong consensus that commissions created perverse incentives.

> *"I just think that the commission structure is really driving the wrong incentives and the wrong relationship."*

> *"There's no rational reason to have a commission. This is completely irrational, it is ludicrous. So it's just offensive, to be honest, that it is that way. And in a professional services environment, how does this incentivise them to give you a good service?"*

Many participants felt managers were unmotivated to secure competitive premiums and there was a direct conflict between owners' interests and managers' financial incentives. There was an awareness that a principal-agent problem persisted in this industry.

> *"Not only is this completely bizarre in terms of a principal agent relationship, it's also completely bizarre in terms of how you would organise an industry."*

Multiple participants explicitly stated they do not trust their managers, particularly with insurance and affiliated services. The annoyance at this breakdown of trust was very evident.

> *"I don't get kickbacks when I do my job."*

One participant undertook some research after the ABC reporting and found there was a relationship between their management company and the nominated broker. They confronted their manager and were told there was no relationship. For this participant, the lack of transparency was more problematic than the practice of receiving insurance commissions.

"I'll start to ask manager about it. She says, oh, no, no, we're lucky. That's not us. That's all Netstrata. We haven't got any relationships like this. And I don't know if she's just dumb or just, you know, barefaced lying. So while I'm really angry about paying the commission, I'm less angry about paying the commission than I am about not being able to trust the agent."

3. Power dynamics and market failures

Some of the participants had negotiated arrangements where managers did not receive a commission, others were struggling to negotiate such terms. This struggle manifested because their current manager insisted on an insurance commission-based agreement or the scheme was dealing with other complex matters (e.g. building defects) and they felt it was too difficult to change companies. In regional areas, this problem was exacerbated due to the limited choice in management services.

Information asymmetry was evident where participants didn't really understand what was industry standard or practice. They did not know what questions to ask to help them understand these arrangements, the potential outcomes for their owners corporations, their rights and options and or how they could evaluate service quality.

When participants were asked if they had made enquiries about the types of services the insurance commission was subsidising, the majority had not enquired or even thought about enquiring.

"I guess that would be a question that we would have to ask. And we didn't know that that question exists."

"My assumption was that it was their remuneration. It wasn't applied to anything."

"I think they just said it was a reduction in the fee."

One participant explained their knowledge came from an informed committee member who understood and worked in insurance. This participant explained how valuable it was to have an experienced person assisting and also how critical it was to their understanding:

"I think that's really key, having people who have some sort of experience and expertise, because half the time you don't even know what questions you ask. You don't even know where to find information or even key search words. It just takes too long and you just, just, Yeah, things move on and you, you feel like you're just stumbling around in the dark."

Many discussed how complicated the fee structures were and how difficult it was to evaluate service quality.

"We should be ensuring that our strata managers are actually giving us service. And all of this stuff just complicates matters. Just justifying that fee, or not. And how do we determine if that service is better than that service? And to me, that's the fundamental issue. You've got no freaking idea if A is better than B at all, because A, you don't even know what the questions are to determine what is A versus B. And then you have all of these smoke and mirrors in the background and people saying, well, I don't charge enough, so I've got to charge more on this in commission. What a load of crap. You either provide a service or you don't."

4. Affiliated entities and pressure tactics

Many of the participants explained that the ABC expose of the strata management industry had been the catalyst for them to make enquiries regarding associated and affiliated entities. For some, independent enquiries made them aware, for others it was via accidental disclosure. Although many were wary of some arrangements, they felt that these relationships had been largely concealed.

As detailed by one participant:

> *"… unfortunately, not at the time of committing to the strata manager. I found out later through the ABC expose. So, yes, I could go back and recall instances where I thought it was odd. You know, why are we going this way? Why is it so expensive and so forth? And I didn't understand that they, the company itself had its own brokerage. There was no transparency. There was no disclosure."*

Most participants experienced pressure to use the services of affiliated companies or companies that the strata manager preferred including insurance brokers, maintenance companies, engineers and builders, legal firms, and debt collection agencies.

As this participant commented, they felt their manager pushed insurance brokers on to them and didn't understand with the limited insurance options available why brokers were needed. There were suspicions that managers pushed for owners corporations to commence claims to increase premiums and in turn commission revenue.

> *"I don't see why we all should be pushed through brokers. In New South Wales, there's very few insurance companies."*

> *"We are our own worst enemies also because there's a lot of strata committees that are pushed by strata managers to put almost every repair in a building through as an insurance claim. Now, that's feeding through to our increased premiums as well. Every time you activate a policy, your premium goes up next time around. So I think, you know, we were our own worst enemies there."*

One participant described fighting with their managing agent who had obstructed the services of the owners corporations preferred supplier to use a subsidiary company.

> *"Being pressured doesn't begin to describe the battle we had with a company which turned out to be 100 per cent subsidiary. The way we found out about it was we had a problem some years prior. We got that sorted and we liked the people we were with and we stayed with them for a long time. Each year we'd get a quote from them. The way we discovered that our inspection was being booked in with somebody else was that that company was told that we had rejected the quote. And they contacted me and said, what have we done wrong? You know, we've been doing this for 10 years, you know, how did we upset you? And I said, what do you mean? I haven't even seen your quote yet. I was smelling a rat by that time, I paid for a business license check and found out they're 100% subsidiary."."*

Many participants suspected the pressure to use particular companies indicated a relationship or beneficial connection. One participant felt pressured to use a strata finance company to fund a large defects matter. They believed the finance company and strata management firm were aligned. They were aware that a commission was being received and rightly or wrongly assumed an association. Similarly, a participant raised questions about affiliations with banking institutions.

> *"When you go to place your funds that are sitting in your working capital accounts, and there must be billions across the whole industry, you get below market rates, and you can't shop around for competitive rates. But I haven't yet got to what the formal arrangement is between the managing agents and the bank."*

Another participant discussed being pressured to use a particular law firm:

> *"We changed our strata manager a couple of years ago, and at the very first AGM that he was holding for us, there was a proposal in there that we would use [named law firm]. And we obviously did not allow that."*

5. Financial impact on vulnerable schemes

Many participants had been involved in major building defect work in their scheme. It was evident that increased insurance premiums and commissions pressure to use certain engineers, builders, and financiers added to their distrust and frustration with their managers.

This sentiment was expressed by the following participant:

> *"We had major works ongoing that was required and the insurance company were well aware of it and water ingress, we got down to only one insurer that was prepared to insure us. And their price was just getting more and more and more and more. And, of course, the broker and the agent couldn't care less because they were making more and more money."*

3.0 Findings conclusions

The findings from the research phases illustrate the complex relationships and practices within strata management that give rise to conflict of interests. The initial unstructured interviews (Phase 1) provided a pathway for further exploration by identifying conflict of interest risk areas which included commission-based arrangements, developer consulting work, affiliated and associated entities, training and sponsorship arrangements, staff remuneration schemes, supplier / service provider referral fees, banking/software integration arrangements and gifts.

Phase 2 provided insights into the types of services promoted by strata management firms (website analysis) and the types of arrangements that are disclosed in strata management agreements. Aside from strata management services, operators also promoted services relating to developer consulting work, building or facility management, and real estate. The most common disclosures related to insurance and broker commission arrangements, energy commissions, training and education, and associated and affiliated entities. Very few made disclosures relating to finance and banking, general compliance, developer consulting and gifts.

Phase 3 explored the findings from Phase 1 in more detail and focused on the impacts that the ABC reporting had on firms, operator diversity, and metropolitan and regional variations. The most diversity in terms of views in this phase related to insurance commissions.

The final phase provided insights into the knowledge and positions held by strata lot owners. General patterns emerged from this phase that emphasised issues relating to transparency, trust, power imbalances, suspicion regarding associated and affiliated entities, and principal/ agency problems.

Part 3: Discussion and conclusions

The findings from this research reveal a complex industry ecosystem characterised by systemic conflicts of interests and fundamental business model dysfunction. The research demonstrates clear patterns of problematic practices while also identifying emerging reform movements and ethical operators working within a tainted system. The findings suggest that while industry reform will be disruptive it is both necessary and achievable. Early adopters have already demonstrated there are alternative business models that better serve strata owner interests. The evidence supports policy intervention while highlighting the complexity of implementation across diverse market conditions.

This part of the report sets out eight discussion categories, illustrating the complexity of conflicts of interest in the strata management industry. It identifies the origins of the problem, addresses the need for change, educates the industry and others on inherent conflicts of interest and identifies reform pathways.

3.1 Historical context and industry evolution

3.1.1 Decades of unaddressed concerns

Conflicts of interest risks in the strata management industry have been documented since the early 1990's. The Alliance Strata Management media expose and subsequent legal case marked the first real warning that a remuneration model had been created that undermined the sanctity of the agency relationship. It was a model that placed profit over duty. Even after repeated warnings by strata legal experts and scholars, the risks inherent in this model continued to be ignored for decades. Thirty years on, the catalyst for change has come from a campaign by the ABC and sustained public and regulatory attention.

3.1.2 Structural factors creating high conflict of interest risk

Strata managers are necessarily placed in a position of power, reliance, trust and authority due to the nature of the agency relationship. The complexity of the legal framework that regulates owners corporations and the reliance on volunteer committee members with limited expertise requires those with specialised knowledge to manage many tasks to ensure that owners corporations function. The burden placed on strata managers to fulfil this position also comes at an additional cost. The cost is that ethical and legal duties are imposed that prevent them from acting in a manner where their own interests are elevated above their clients (as the principal). These duties are imposed because principals are in a more vulnerable position due the structure of the environment and agents are presented with and can create opportunities that benefit them. In strata management, these opportunities often arise due to the dependency on multiple external suppliers and service providers. The imposition of best interest duties should preserve this special relationship and repel arrangements that might undermine it. The very nature of strata management makes it a high conflict of interest risk industry. The relationships and practices that give rise to conflicts of interest, as outlined in this research, show that many in the industry have been unable to successfully resist opportunities that reward.

In addition, if a manager has been delegated owners corporation functions or has been appointed to administer the owners corporation a higher standard should be applied. The owners corporation is in a more vulnerable situation under these conditions and special care is required by managing agents when making decisions on their behalf. It is in these situations where opportunities of self-interest are taken and go undetected.

3.2 Conceptual framework and regulatory environment

3.2.1 Definition and recognition challenges

The strata management industry has embedded and normalised a conflicted remuneration model and the structure has become institutionally entrenched. This compromises a manager's ability to objectively assess their duties to act in the best interests of their owners corporation clients. This was evident in the interview phase where traditional operators and to some extent transition-oriented operators framed their responses to critical conflict of interest questions in terms of remuneration impacts. Their concern relating to law reform was focused purely on financial impacts – both to lot owners and their business. The reform-oriented operators framed their responses in terms of ethical risk and the need to move away from pre-existing conflicted practices. The divergence in perspectives may come from the inability of some managers to understand or appreciate the legal and ethical duties that bind them.

To some extent, this is unsurprising as conflicts of interest is a complex area to easily decipher. Adding to the complexity are inconsistent terms, variations in regulatory frameworks across

jurisdictions, overlapping duties in various sources of law, and the integration of both ethical and legal standards.

It is important to reiterate that conflicts of interest are not necessarily bad and are an inherent feature in industries like strata management. As explained in this paper, the threshold for what constitutes a conflict of interest is low – just being tempted to ignore your duties is sufficient to be in a conflict of interest situation. There will always be an occasion where a manager is tempted by a benefit. The real risk comes afterwards when a manager places themselves in a position where they are unable to discharge their legal or ethical duties. An acceptance that conflicts of interest exist in this industry is important so mitigation and management strategies can be implemented. As highlighted, evading or escaping conflicts of interest are the best strategies that can be employed. Exposing (or disclosing) is more problematic as a strategy. However, if the aim is legal compliance then following the disclosure rules in the relevant legislation and the rules for informed consent (full and frank disclosure of all the material facts) is all that is required to fulfill fiduciary obligations. However, it does not alleviate the ethical risk and may not provide any security for owners corporation clients in terms of perception, trust and value.

Legal compliance should be viewed as the minimum standard in terms of conflicts of interest.

3.3 Current industry practices and business models

There are strata industry practices and relationships that have been identified as potential conflict of interest risks. It is likely there are other risks yet to be uncovered. Some of these known practices and relationships are more widespread than others. For example, the receiving of insurance commissions and the use of Schedule B (or additional service) fees as staff incentives or bonuses. Integrated businesses or affiliated entities are less prevalent in mainstream management but are regularly incorporated into larger firms. Each of these practices and relationships will be discussed in turn highlighting the nature of the risk, the severity of the risk, and mitigation and management strategy options (if available).

Criteria for assessing the severity of conflicts of interest have been formulated by Lo and Field.[68] The likelihood of undue influence and the seriousness of the consequences / possible harm frame the assessment. In terms of the likelihood of undue influence, three questions need to be asked:

1. What is the value of the secondary interest? There is a general assumption that the greater the value (e.g. size of the financial gain), the more probable is the influence. There may also be increased influence when the economic value is low (e.g. a small gift) but it sustains a relationship.
2. What is the scope of the relationship? The duration and depth of the relationship is key here. The longer and closer the relationship the more likely the influence.
3. What is the extent of the discretion? This questions the latitude that the duty-bound person is afforded. The level of delegation or the appointment of a manager as an administrator increases influence and risk. The extent of oversight is also an important factor here.

In terms of the seriousness of the possible harm, two questions are relevant:

1. What is the scope of the consequence? The consequence(s) need to be articulated for the duty-owed person.

[68] Lo, B., & Field, M. J. (2009). Principles for identifying and assessing conflicts of interest. In *Conflict of interest in medical research, education, and practice*. National Academies Press (US).

2. What is the extent of accountability? Conflicts of interest are more serious when the level of accountability is less extensive. If there is a review of decisions by other independent persons or authorities, there is generally less harm

3.3.1 Insurance commission dependencies

The research highlights that many strata management companies depend on insurance commissions as a revenue stream. For some, the commissions represent the company's annual profit, for others it is revenue used to cross-subsidise management services. As a result, larger schemes or schemes with high insurance premiums are effectively subsidising smaller schemes or schemes with low insurance premiums. This has created a distorted and inequitable remuneration model.

A central issue discussed in this research was related to insurance brokers. There was confusion about the broker appointment. Some managers believed the broker was almost an extension of their role and that it was up to them to choose a broker. Others believed the owners corporation was the client of the broker. However, according to interviewees, it was rare for a motion at an annual general meeting or committee meeting to include the terms and conditions (including services and fees) to engaging a broker.

Many interviewees believed they had the authority to engage a broker on behalf of the owners corporation. However, it was questionable whether the delegation as described both in the legislation and in agency agreements extend that far. The *Strata Schemes Management Act 2015* (NSW) (s. 13) sets out the functions that may be delegated to a strata managing agent. The most relevant relating to insurance is s. 13(1)(e) - the taking out of insurance required or permitted by this Act. It is a stretch to think the delegation would extend to the engagement of an insurance broker.

The confusion regarding engagement might arise due to the *Strata Schemes Management Act 2015* (NSW) (s. 166) which places an obligation on the strata managing agent to provide the owners corporation with no less than three insurance quotations. This provision is at odds with the principal/agency relationship and the other provisions that place an onus, rightfully so, on the owners corporation to manage its scheme. In any event, the broker appointment process lacks transparency and arguably proper authorisation.

3.3.1.1 The conflict of interest risk

This model presents two primary areas of concern.

The first involves the compensation structure for strata managing agents, who receive commissions funded by their own clients. These commission rates appear arbitrary and lack clear correlation to the insurance services provided. Furthermore, owners corporations end up bearing additional tax costs on these commissions, which are embedded within their insurance premiums.

Compounding this issue, cross-subsidisation practices create a situation where the commission arrangement favours certain owners corporations (such as smaller schemes) at the expense of others (such as larger schemes) within the same portfolio. This is despite the managing agent having fiduciary obligations to all parties. This represents a fundamental conflict of interest, with managing agents failing to prioritise their clients' best interests.

The second concern arises when commissions are directed, wholly or partially, to insurance brokers. In these situations, strata managing agents may be incentivised to advance the broker's interests rather than their clients'. This risk is amplified by the fact that insurance brokers frequently employ the same cross-subsidisation approach.

3.3.1.2 The severity of the risk

The influence of commissions is high due to the size of the financial gain (interviewees explained commissions can make up 15-25% of their revenue). This is exacerbated when the agent uses their delegated authority to place insurance and engage an insurance broker.

Possible harms are not inconsequential for many owners corporation clients particularly those with high premiums.

3.2.1.3 Mitigation / management strategy options

It is difficult to devise a mitigation strategy that allows the commission structure to remain. The complexity of these arrangements makes effective disclosure difficult to achieve.

It is noted that financial services licensees and representatives (for this discussion includes, insurance brokers), are now required under the *Corporations Act 2001* (s. 963BB) to, inter alia, seek informed consent from a client if personal advice is given in relation to a financial product (e.g. insurance) and a monetary benefit is received (including commissions). Although this is a mitigation step, it may not absolve the ethical conflict of interest risk completely. If clients are unable to comprehend and evaluate the services provided or the cross-subsidisation method utilised, the risk remains.

3.3.2 Developer consulting arrangements

The research identified that although managers undertake developer consulting work (pre-registration), for most it was a service offered but not pursued with any regularity. For many of the interviewees, there was an acknowledgement that relationships with developers cause problems post-development leading to high levels of distrust with owners. Even the traditional commission dependent operators, found these types of arrangements challenging to manage due to the conflicted relationship.

Generally, this type of front-end structuring work is performed for free or below commercial rates with revenue being recovered through initial appointments, the issuance of information certificates (e.g. section 184 certificates in New South Wales) to new lot owners, and insurance commissions. As highlighted in the findings, aside from general pre-registration tasks, managing agents provide strategic structuring advice that enables ongoing developer control. This advice can be detrimental to the incoming owners creating competing loyalties. Control that often leads to conflict between the developer (or its associated entities) and the owners corporation. This is particularly apparent if other serious issues (e.g. building defects) arise. Similarly, and as addressed in previous research, lowballing of levies where the developer pressures the agent to create a low-cost budget for the initial year post registration, continues to be a problem.

3.3.2.1 The conflict of interest risk

As previous research has highlighted, these types of arrangements create conflicts of interest. The temptation to ignore duties is high especially when managing agents have a pipeline of future work coming from a developer. Strata managers cannot place themselves in a position that promotes third party interests or their own over that of their owners corporation client. It is in the best interest of the developer but not the owners corporation (even if it is yet to be created) to keep budgets and levies artificially low, to get advice on structures that either enable them to retain control (where the control is disadvantageous to the future owners corporation) or ensures future revenue streams, or impedes the building defect rectification process (including influencing the use specific contractors).

3.3.2.2 The severity of the risk

The severity of the risk of this relationship is high because the financial incentive is substantial. It includes the value of the structuring work – certificate fees, commissions, a potential pipeline of future work, and the ongoing management fees. In addition, the duration and depth of the developer/agent relationship is a factor that needs to be considered when assessing influence. If the developer/agent relationship is longstanding (that is, the agent is the preferred consultant for a particular developer) the influence risk is more acute. These business relationships (whether ongoing or not) commence many months or years before the owners corporation is formed and any future owner is known. The developer relationship is well established before the secondary relationship exists. Switching loyalties from an established relationship to a new one is a difficult hurdle to overcome. It is arguable that even though the owners corporation is not established during this period, the agent owes duties to the future owners corporation if there is an arrangement (formalised or not) that the agent will be appointed. The control the developer has as the original owner in the initial period post-registration provides the agent with discretion and therefore influence.

The potential harms are more serious in relation to this conflict of interest situation than any other. The consequences that flow from the competing interests (stymied building defect work, lowballing levies, unfair building management contracts, structures embedded that allow for developer control (leases etc)), can lead to financial and safety risks in the short and long term for the owners corporation.

3.3.2.3 Mitigation/management strategy options

It is acknowledged that strata managing agents are well placed due to their skills and expertise to undertake pre-registration work for developers. The only way to effectively mitigate any conflict of interest would be for the arrangements to exclude an initial management appointment. That is, strata management companies (or any affiliated entity) should not be appointed to an owners corporation post registration of the scheme. It is the only ethical pathway that eliminates these conflicts of interest risks. If, due to the remote location of the scheme or the complexity of the scheme, choice is limited in terms of management, an independent third party should be consulted to evaluate the situation. This third party would place parameters around the appointment to limit any conflict of interest exposure.

3.3.3 Vertical integration and affiliated entities

The research highlighted that complex integrated service models were mainly incorporated into larger firms. The types of associated entities varied from maintenance, plumbing, insurance broking, remedial work, legal, valuation, insurance, property, tax compliance, fire protection, and energy broking. Although these larger firms disclosed (often in very small font) the basic nature of these relationships in their management agreements (e.g. related party, subsidiary), detail regarding the association was lacking. In some regional areas, associated entities have been created out of necessity due to limited supplier availability. There appears to be a different dynamic in play, one based on need not necessarily profit.

Management agencies may not directly receive a financial benefit from the engagement of the associated entity by the owners corporation, but a related party benefit (e.g. director, shareholder, family or friend).

These associated connections impede a managing agent's ability to maintain arm's length transactions which is a concern.

3.3.3.1 The conflict of interest risk

These relationships present a conflict of interest as the very nature of the structure (the purpose of their creation or inclusion) is for those associated with the managing agent to financially benefit from the manager's client portfolio.

In addition, there is an inherent danger that managing agent could exploit their privileged access to independent quotes to advantage associated entities, creating a conflict of interest that undermines competitive tendering.

3.3.3.2 The severity of the risk

Given the high level of compliance and reliance on external suppliers and service providers in the strata industry, the financial rewards that flow to any associated entity are likely to be sizeable. When assessing the scope of the relationship, each arrangement would need to be evaluated. However, the longer the association or the closeness of the parties (e.g. family) the stronger the influence. In instances where the managing agent has delegated authority to engage suppliers and service providers or where they have been appointed as an administrator, influence is likely to increase. Oversight is key to lowering the risk threshold.

There may be instances where the services provided by an associated entity are of the highest quality and the fees charged are fair and reasonable. In these circumstances the seriousness of the harm may be lessened.

3.3.3.3 Mitigation/management strategy options

The only mitigation strategy option is implementing independent third-party assessments to ensure that the services and fees are competitive and the quality of services are comparable to other suppliers and providers in the market. Informed consent from owners corporation clients should be required prior to any engagement and managers should not use any delegated authority to automatically action such engagements. However, it is an ethical slippery slope and managing agents should avoid these types of arrangements and relationships.

3.3.4 Staff remuneration structures

The research highlighted that it was common practice for staff managers to be paid a base salary and a percentage of Schedule B (or additional service) fees as part of their remuneration. These arrangements were borne out of customer expectations requiring managers to attend owners corporation meetings outside of normal business hours. This commission arrangement incentivised managers for the long hours needed to fulfil the role. Overtime, the structure incorporated other services including managing building defect issues. There were mixed feelings from interviewees regarding this practice. Proponents thought that as licensees, they had a responsibility to ensure that Schedule B billings were accurate and reflected the work and time required. Opponents of the practice could see unintended consequences including overcharging clients.

3.3.4.1 The conflict of interest risk

The practice of tying schedule B billings to staff compensation has created a conflict of interest risk for strata management agencies. The risk manifests because of the temptation to overcharge for services. As explained by interviewees, there are management firms that have implemented minimum billing thresholds for staff. As reported, the lack of oversight by owners corporations has allowed some firms to take advantage when billing additional services.

Managers universally described the market pressures to maintain these practices due to competition for staff.

3.3.4.2 The severity of the risk

The value (e.g. 50% of billings) creates a sizeable financial benefit for staff managers. The risk is greater in circumstances where the management firm has delegated authority to pay (themselves) for additional services. It is not a common practice in the strata management industry to issue monthly (or regularly) invoices to owners corporation clients for these services and await approval prior to payment. The accessibility to funds and the common delegation to pay invoices substantially increases the severity of the conflict of interest risk.

The harm caused is that owners corporation clients are potentially paying for services not required.

3.3.4.3 Mitigation/management strategy options

It difficult to envisage a strategy that mitigates the potential risks caused by this practice. It is appropriate that owners corporation clients pay for required services and additional or premiums fees for meetings held outside normal business hours or distant locations. It is also appropriate for companies to reward employees with bonuses, if they choose. These bonuses should not however be tied to billing. Company oversight is an effective mechanism if auditing protocols are in place to ensure overcharging and overservicing are restrained. In addition, providing owners corporation clients with a monthly itemised invoice of these additional services is a must to lessen the conflict of interest risk.

3.3.5 Supplier/service provider relationships

There is a heavy reliance on suppliers and service providers in the strata sector. The strata managing agent is the conduit - facilitating, referring and recommending suppliers/providers to the owners corporation. It is this tripartite relationship (two parties have financial business interests) that has led to arrangements where in exchange for work (or an opportunity), suppliers and services providers offer a benefit to the managing agent. These arrangements range from kickbacks (where a percentage is paid to the managing agent) to more subtle benefits (opportunity to correct financial statements (auditing) or provision of free or reduced software fees).

3.3.5.1 The conflict of interest risk

It is more difficult to assess the extent of conflict of interest risks in some of these practices. Some are straightforward, for example, a percentage referral fee (kickback) although it is a practice that may be less visible. Other more complex arrangements make it difficult to examine whether managing agent interests are being served over those of their client. The lack of transparency of some of these arrangements is cause for concern.

3.3.5.2 The severity of the risk

The value of the secondary interest is difficult to determine and dependent on the agreements made between the parties. For large portfolios, the value may be substantial. As highlighted in the McGrathNicol Report[69] on Netstrata, payments were received by third party contractors or suppliers totalling over $1 million during the relevant period (being 1 January 2022 to 27 March 2024). Similarly, if there are any benefits derived from software providers (e.g. free or lower service fees) because of client funds (collectively) being held in banking institutions (due

[69] https://www.nsw.gov.au/departments-and-agencies/fair-trading/news/nsw-fair-trading-releases-mcgrathnicol-report-into-netstrata

to integration), managing agents' conflict of interest risk is heightened. This is particularly relevant if another banking institution would provide interest on transaction accounts.

The potential harms are that owners corporation clients may be paying more for supplier services (including compliance reports) or not receiving a financial benefit.

3.3.5.3 Mitigation/management strategy options

There is no appropriate strategy to manage supplier/service provider kickbacks. These should be eliminated.

As recommended in the McGrathNicol report, managing agents should rotate auditors and consider using a panel of randomly selected auditors. Further, auditors should report in the first instance directly to the Treasurer or other nominated committee member before sending the auditor's report through to the managing agent.

Strata managing agents should ensure that software is being paid directly to the provider and not being discounted due to a bank affiliation.

3.3.6 Training and event sponsorship

As explained by many interviewees, there has been change in the market from suppliers providing training for free to now charging for training services. Although anecdotally, it appears that many supplier companies continue to provide lunch or other benefits to managing agencies in exchange for the opportunity to provide an education seminar. Inhouse event supplier sponsorship (e.g. the Christmas party) appears not to be a widespread practice but nonetheless would be a conflict of interest risk for those agencies.

3.3.6.1 The conflict of interest risk

There is a conflict of interest risk for managing agents that accept free or reduced fee training. The risk arises as there may be psychological pressure to return the favour by recommending the supplier to the client (a feeling of indebtedness). There is a product or brand loyalty bias that is created as the training naturally focuses the agent's attention on the suppliers products or services (limiting objectivity), and exclusive knowledge is created in the supplier's systems or products that may lead to lock-in recommendations. Similarly, conflicts of interest risks arise when managing agents request payment from suppliers for the opportunity to train or provide education services. The risks in these situations are even higher as pressure is applied to clients to use the services of the education sponsor (as they seek a return on their investment).

3.3.6.2 The severity of the risk

Many interviewees were displeased that they now paid for training, which provides some insight into the value of the interest. The harm of these relationships comes from pressure applied to use specific suppliers or service providers.

3.3.6.3 Mitigation/management strategy options

Suppliers and service providers are often well placed to provide training and education that enhances the knowledge base of strata managers. Mitigation strategies could include the disclosure of supplier training, recusing themselves from sole procurement decisions, maintaining a training register, prioritising independent, industry-neutral professional development and when recommending any supplier or service provider who has provided training, disclose the relationship and provide impartial alternatives.

These six broad categories serve to illustrate the extensiveness of the conflict of interest risks facing this industry. Although for many management agencies, only a few of these practices

and relationships are relevant, collectively these risks impact on the professional standing and status of the whole industry.

3.4 Stakeholder perspectives and impacts

3.4.1 Manager categories and positioning

The research showed a diversity of ethical positioning within the management industry. Although the traditional operators that are commission-dependent (or at least wish to retain this source of income) and are defending the status quo make up a large proportion of overall operators, there is a clear shift in the market with managers demanding industry change and law reform. There are the reform-oriented managers who reject commission-based models and have been successful in implementing higher base fee remuneration arrangements. Then there are the transition/conflicted operators who acknowledge the problems, want change but are awaiting a legislative mandate. Their reluctance stems from the competition currently in the marketplace by providers promoting low base fees. The transition operator view is that legislative reform is the only mechanism that will create a level playing field where managers will compete on service delivery.

3.4.2 Owner experiences and knowledge gaps

The owners participating in this research would be best described as highly educated people who currently work or previously worked in a professional setting. Many have a finance, accounting or business background. There were owners who had spent an inordinate amount of time working on their owners corporation committee. Several were dealing with complex issues, specifically major building defect works. Unsurprisingly, these owners were concerned about conflicts of interest which is why they accepted the invitation to be involved in the research project.

The findings of this phase highlighted that owners understand managers receive an insurance commission but lack knowledge of commission structures and processes including tax implications. Owners were unaware of portfolio cross-subsidisation effects and the unveiling of this common practice only led to further suspicion about the industry. Owners included in more vulnerable schemes (with defects) felt disproportionately impacted by the commission structure. The consensus was that remuneration models should be based on fee for service. The convoluted remuneration structures made it difficult for owners to effectively evaluate the services provided by managing firms.

Considerable concern was raised about managing firms that were tied to other entities including insurance brokers. Overall, trust erosion due to a lack of transparency and perceived deception was high.

It is apparent there has been a fundamental breakdown due to these common conflicts of interest that have created an agency problem. Feedback from these owners should signal to the industry and governments that inaction regarding conflicts of interest has created, and will continue to create, a discordant environment between managers and owners.

Undoubtedly, there will be concerns by some strata lot owners that the removal of insurance commissions will lead to increased management fees. This is a likely outcome given the common practice of portfolio cross-subsidisation and the possibility that insurers may increase costs. Unfortunately, this might be the price paid for the institutionalised conflicted remuneration model created by the strata management industry decades ago and the highly regulated environment. Rules regulating these dealings must apply to all, that is the nature of strata.

3.5 Disclosures failures and transparency illusions

Disclosure, as a regulatory tool, has muddied the waters in terms of ethical practice. The use of disclosure as a defence has placed the duty-bound (strata managers) in an ethical blackhole. The use of disclosure has diluted the sanctity of the principal/agent relationship and the strict legal duties that flow from that relationship. In turn this has created an environment of distrust (whereby the principals distrust their agents) and justifications/defensiveness (where the agent believes they are justified in effectively breaching their duties).

Information disclosure has been an embedded regulatory tool used in multiple legal environments for decades – it is an easy mechanism to embed as it places responsibility on the duty-owed or advice receiver to take responsibility even in the face of market exploitation. What lawmakers have not understood, is the complex nature of some of these relationships and practices, deficiencies in human mental processing, and the potential harms (for both parties) that result.

An assessment of the current regulatory disclosure regimes has been lacking. More specifically, whether the content of the disclosure achieves the level of transparency required for an owners corporation client to fully appreciate the arrangement subject to the disclosure. To be effective, there needs to be an assurance that the information disclosed is comprehensible, doesn't mislead the client, is accessible and is presented in an easily digestible format. Inserting clauses in an agency agreement (including as fine print) would not pass a basic test.

In any event, there are other disclosure limitations that prevent this tool from being supported. Although disclosure with effective consent is a defence for a fiduciary breach, the consent element is not a requirement in most other disclosure regimes. The owners corporation client is not approving or agreeing to these arrangements. Even if the laws were to change, requiring effective consent, there are still problems to overcome.

There are numerous psychological barriers that impede the effectiveness of information disclosures. For duty-owed (owners corporation clients), there are difficulties with judgmental correction. Owners may know to be on alert or cautious (because a practice or relationship has been disclosed) but they don't often have the motivation or knowledge to determine the likely effects of the disclosure (the severity of the risk). This means they don't know how cautious they need to be or what steps they need to take. Further, if a client likes their managing agent or considers them ethical (because they have been upfront and honest about the conflict of interest), it may serve as an assurance that nothing untoward will occur, which heightens trust. People often want to maintain harmonious relationships, so to avoid confrontation or ill feelings, they may simply comply and agree.

For the duty-bound (managers), conflict of interest risks can be evaluated differently. For some, the rewards or benefits gained may not be worth taking because they understand the sanctity of their duty and the potential reputation fall out if exposed. For others, a self-serving bias exists. We regularly hear justifications (and rationalisations) from managers that they are owed more because of the complexity and onerous nature of the work they undertake. Regularly statements are made by managers that they don't get paid enough for the work that they do. In turn, rewards and benefits gained by participating in these conflicted practices and relationships appear to reconcile their value. Disclosure in these circumstances does not appear to be the method that cures the conflict.

3.6 Market failures and power dynamics

The origins of these exploitative practices and relationships stem from the low base management fee model created in the 1970s. The model is so ingrained it has created numerous principal-agent problems. There are misaligned incentives, delegated authorities are used to benefit managers over owners, owners corporations lack expertise to provide effective oversight, and distrust in the industry is widespread.

3.7 Industry responses

There is resistance to change from many in the industry. The concerns relate to the banning of insurance commissions. There are fears that businesses may no longer be viable and that consumer costs will increase placing additional burdens on many consumers. For those resistant to change, there is a belief that disclosure (particularly the more detailed disclosure regime in New South Wales) is sufficient and that time is needed to evaluate its effectiveness. Transition operators are waiting for guidance from the government by way of mandated action. These operators are reluctant to undertake voluntary reform in a market where pricing is so competitive.

However, in the wings are the reform operators who have created best practice models that, to a large extent, have eliminated conflicted remuneration structures. They have developed sustainable and viable pricing models and they use effective transparency as their competitive advantage. Their dealings with suppliers are at arm's length and they are focused on quality service delivery.

3.8 Key findings and conclusions

3.8.1 Systemic industry dysfunction

The research reveals that conflicts of interest are not isolated incidents but represent a fundamental structural problem that has been institutionalised over 30+ years. The industry has created a business model where profit systematically conflicts with legal and ethical duties, creating what the research describes as an "ethical blackhole."

3.8.2 Failure of current regulatory approaches

The research conclusively demonstrates that disclosure-based regulation is a flawed mechanism. Disclosure has created an illusion of transparency. The complexity of arrangements makes meaningful disclosure in many instances impossible to achieve. There are also psychological barriers that prevent effective disclosure even with consent, and disclosure has become a shield for unethical practices rather than a protective mechanism.

3.8.3 Categorisation of industry participants

The research identifies three distinct operator categories, revealing an industry in transition:

- Traditional operators: are commission-dependent and actively resisting change;
- Reform-oriented operators: have successfully implemented ethical, fee-for-service models; and
- Transition operators: recognise problems but fear competitive disadvantage without a legislative mandate.

3.8.4 Policy implications

Although some of these areas have already been considered in New South Wales, all state and territory governments should commence legislative reform processes (if relevant) that:

1. Prohibit insurance commissions: there should be an outright ban rather than further attempts to manage these types of commissions through disclosure. Although the focus of this report has been on strata managing agents, the ban extension should include insurance brokers. The cross-subsidisation approach creates inherent conflicts that cannot be mitigated.

2. Separation of developer consulting and management: companies providing pre-registration consulting should be prohibited from initial management appointments. This is the only way to eliminate the severe conflicts arising from competing loyalties.

3. Place restrictions on affiliated entity dealings: there should be processes in place that require independent third-party validation for any related party transactions, that prohibit the use of delegated authority when engaging affiliated entities, and mandate competitive tendering processes with independent oversight.

4. Reforms delegation powers: there needs to be limits on the scope of delegated authorities particularly for financial decisions. There needs to be explicit owners corporation approval for insurance broker appointments and supplier engagements.

It is important to note that although this research has predominantly focused on NSW, the practices and relationships outlined and the associated risks are areas of concern for managing agents in every Australian state and territory.

3.8.5 Industry implications

1. Pricing model changes: the strata management industry needs to shift to fee-for-service or other transparent pricing model. The management fees will need to increase to compensate for lost commission revenue. Itemised monthly invoices should be sent to owners corporation committee treasurers or other nominated members for approval prior to payment.

2. Professional development requirements: the industry must invest in genuine professional education and training with an emphasis on ethical decision-making. In addition, there needs to be the development of industry-specific ethical guidelines and best practices. The current (new) code of ethics developed by the Strata Community Association should be reviewed and redrafted.

3. Enhanced accountability mechanisms: strata management businesses should consider implementing procedures that ensure there are auditor rotations with direct reporting to owners corporation committees and regular independent review of management practices.

3.8.6 Stakeholder impacts

1. For strata managers: there needs to be a rebuilding of trust through transparent and ethical practices and investment in new business models and pricing structures.

2. For owners corporations: there needs to be a recognition that strata management fees will increase and that the short-term discomfort will lead to long-term value through aligned incentives. Owners corporation members must engage in education to enhance management relationships, and there needs to be a greater involvement in decision-making to ensure proper oversight.

3. For the broader industry: suppliers and service providers must develop arm's length relationships. To enable the strata management industry to transform, incentives that undermine the manager's legal and ethical duties need to cease.

3.8.7 Critical success factors for reform

1. Legislative mandate: the research clearly shows voluntary reform will not succeed due to competitive pressures. Government intervention is essential.
2. Transition support: both managers and owners will need support during the transition. This should include clear and considered timeline implementation, industry guidance, and consumer education programs.
3. Enforcement mechanisms: new regulations must include meaningful penalties for non-compliance, regular auditing and monitoring, and clear complaint and resolution processes.
4. Industry leadership: reform-oriented operators should be recognised and supported as they demonstrate viable alternative models. Management businesses need industry bodies to provide support during transition with meaningful engagement.

Conclusion

The research suggests that while reform will be disruptive, it is both necessary and achievable. Early adopters have already demonstrated that ethical, profitable business models are viable. The key is creating a level playing field through regulation that prevents a "race to the bottom" in pricing and ethics.

The fundamental message is clear: the strata management industry has reached a critical juncture where the institutionalised conflicts of interest have eroded trust to such a degree that only comprehensive legislative reform can restore the integrity of the principal-agent relationship that should be at the heart of strata management.