Give yourself room to manoeuvre

Pitfalls abound for the unwary strata investor so educate yourself before signing a contract and be bold in your demands.

Ben Hurley

More than one-third of new homes built in Australia are now apartments. For investors, they are relatively affordable, they usually offer higher rental yields than houses, and newly built homes give tax breaks for depreciation.

But they also have a set of risks that people accustomed to dealing in houses need to be aware of.

Apartment owners' corporations usually appoint a building manager to look after ongoing maintenance issues.

It was once commonplace for the developer of a building to lock in a 10-year management contract, which could be on-sold to another management firm without the permission of the owners.

That's less common these days after various law changes that mean owners in a new apartment block have to approve any contracts entered into before the first general meeting.

Strata commentator Jimmy Thompson, who runs the website flat-chat.com.au, says the key issue now is to watch what you sign.

"The developer and their friends will present a very convincing case of why you should just let things roll," Thompson says.

He warns that naive new owners sometimes sign up to decade-long contracts, which may contain a resale agreement, and effectively mean owners forfeit the right to hire and fire a shoddy management firm.

What owners should do, he says, is demand the contracts are held over for three to six months until an executive committee has been formed and has looked at the contracts in detail.

A big area to watch is lifts – in which understandably few have any expertise. It is hard for new owners to resist when presented with a 10-year lift maintenance contract from a reputable firm.

Strata manager David Morris says the contracts sometimes have hidden tricks. Lift maintenance may cost $10,000 a year, and a typical warranty is one year. A second "free" year may be offered to make a contract sound more attractive, but in the small print the cost of yearly maintenance may climb to $12,000 a year for the last eight years.

A bigger area of concern in his mind is ensuring the building's waterproofing and fire safety equipment are up to standard. State laws vary but buildings over three storeys high usually don't have home warranty insurance.

This means that if defects are discovered outside the building's warranty period, the owners have to sue the developer to get them fixed. Morris says sometimes defects are hard to pick up in a new building, so your solicitor should ensure your contract has warranties.

"The private certifiers may well say it's compliant [with fire and building codes] and in five years' time you find out it wasn't," Morris says.

Thompson says a quick search of legal website Austlii will tell you a lot about a developer's track record not just for building defects but also about court appearances after trying to avoid fixing them.

Good research is even more important when investing in older buildings that were constructed before safety codes were updated. Councils can order owners' corporations to pay millions of dollars to rectify lax fire standards.

Strata lawyer Stephen Goddard, who heads the Owners Corporation Network, says a look through resolutions in previous executive committee meetings may show whether there are ongoing maintenance issues or fire orders issued by council, which haven't been disclosed in the contract. In these cases, you want to check how much money is in the sinking fund.

"You don't want to be in a building that has to replace every window and not know," Goddard says.

Bannermans Lawyers' David Bannerman says buyers should check what will actually belong to them after they purchase. Parking spaces, seemingly private gardens and even balconies may turn out to be part of common property.

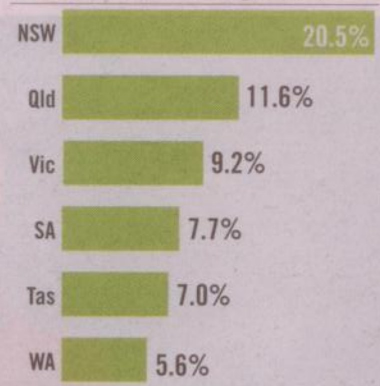
If you are buying with the aim of renovating, check what the procedure is for those works. In some buildings it can require a special resolution and by-law, which takes a lot of time.

And beware of low strata levies.

"A building with unusually low levies probably indicates they are not complying with their obligations to take into account their 10-year plan for their sinking fund," Bannerman says. "There may well be a big special levy later on to do big capital works."

Crowded house

Apartment share of housing (%, 2008)



SOURCE: ABS

Strata title