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YSP Podcast Transcript: Episode 073. The 3 Ways to Fund Your Strata Building - with Paul Morton

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Intro: Welcome to Your Strata Property. The podcast for property owners looking for reliable, accurate, and bite-sized information from an experienced and authoritative source. To access previous episodes and useful strata tips, go to www.yourstrataproperty.com.au.

Amanda Farmer: Hello and welcome. I'm Amanda Farmer and this is Your Strata Property. Paul Morton is the CEO of Lannock Strata Finance. From a symphony orchestra to working in a bank, to a prestigious overseas business school, to then founding Australia's leading strata finance company, Paul Morton has covered a lot of ground and he will be well-known to many of our listeners. He has degrees in music and economics, as well as postgraduate finance and management degrees. Paul is deeply engaged in the strata industry and is acknowledged as the country's subject matter expert in the economics of strata plans. Today I am delighted to welcome Paul Morton. Welcome, Paul.

Paul Morton: Oh, hi Amanda. It's a pleasure.

Amanda Farmer: Lovely to have you with us. We were just chatting off-air about the fact that our offices, I think, are about a block apart, yet we haven't managed to get together for a coffee. This is the first time we're having a chat and it's over Skype video.

Paul Morton: Well, I think that's unusual, but I guess it's either technology or we're both too busy.

Amanda Farmer: Yes, I think it might be the business of the strata sector, that's for sure. But of course I have you on the show to share your expertise when it comes to strata loan facilities, and the Lannock and the name Paul Morton, as I said, will be well-known to many of our listeners. It's an area of the strata world that you have been deeply involved in for a long time now. I want to start by asking you, Paul, why is it so important for people living in strata to know about strata loan facilities?

Paul Morton: Well, it's not just about loans in my view. It's about how you fund important works in strata, and what's right for you and for all owners in their situation. It's critical to know and understand the 3 options there are. You can use a sinking fund, you can raise a special levy, and most people would know about these, but the body corporate can also borrow. So each of these option has their pros and cons, and almost every situation will involve a mix of the 3. With a strata loan, you get the project finished quicker, and that's better for everybody from a lifestyle and a financial perspective.

Amanda Farmer: So you would say that a good financial plan for a strata building would be a mix of those 3 things? Sinking fund monies, raising special levies, and having the option of a strata loan?

Paul Morton: Absolutely. At least all 3 of those need to be considered. So a good financial plan, like any other plan, on the surface it's going to be clear, it's got to be simple and concise. But underneath, you want something which has been really robustly debated. You want to have a highly considered plan. It's got to be rational, highly reasoned, and it's got to be sound logic. Most importantly, appropriate to the situation, because every owner is different. Every owner's corporation is different, so every financial situation is going to different. There's no one size fits all, so you need to work out what's best for you in your particular situation.

Amanda Farmer: What kinds of situations, in your experience Paul, would strata buildings and owners be looking at using a loan facility, as opposed to their sinking fund ... and I should be saying actually under the new law in New South Wales capital works fund, or raising a special levy? What kind of situations are, do you think, suited to strata loan facilities?

Paul Morton: Well actually talking about the New South Wales law, I think changing it to capital works fund might have been partly our doing, because that was the phrasing we used in one of our submissions to the government, and incidentally it's added to be considered every year, and some people are quite confused about this. It's not that you must have a special levy or must have a sinking fund levy, or must borrow. It's that every year in New South Wales, you've got to think about how you want to fund your future capital works budget. I don't have to say that that's really good. The more thought that goes into things, the better.

But you asked me about examples. Look, we've had so many loans, there are so many examples. Throw a dart at the wall and see how we go. But recently we had a building in Randwick. They had a fire order and it required some costly unforeseen works. So they contacted us. We provided a $500,000 loan and they're making the first draw down on that next week. There's another property in Bondi where they're borrowing 300,000 from us to do the first steps on a plan and a DA, to see how they should be redeveloping their building. If they go ahead, if they get the DA, they'll be doing things like turning an existing apartment into a car park.

They'll be putting on balconies. They'll be putting a penthouse on the roof, and overall, they'll be spending several millions of dollars. But it starts with the funding for the DA. Another building in Chatswood has recently had problems, and they'll be starting to borrow $400,000 from us next week. There are so many examples, raising tens of thousands to tens of millions of dollars for anything. For working capital or repairs and maintenance, building defects, litigation, or what's becoming much more important and relevant, particularly in New South Wales, the so-called strata renewal.

Amanda Farmer: Yes. So just to cover off a couple of those examples there, Paul. You mentioned there are unforeseen ... well, what I would call unforeseen works, for example when you have a fire order. My experience of fire orders, when they're issued by councils, they need to be attended to within a short space of time, not only to comply with the order but to make sure that those who are living in and visiting your building are safe. It's not always possible for owners to get together and raise that money themselves.

Not everybody has the security to provide for a loan personally, or the equity in their own homes, so that's definitely been my experience, that I see buildings rely on strata loans when they're doing that sort of urgent, unforeseen work. So I think that's a great example. Then very interesting with that building that you mentioned in Bondi, I think, you said it was, that was just investigating whether the development was going to feasible, and if it is, it's going to be a multimillion dollar development.

But of course, there are some costs involved in those investigations and the original application to council. But rather than sending owners off to go and raise the money separately against their own lots for the funding of that investigatory work, then that's something that a strata loan can step in and fill in that gap. So I think that's a really great example as well.

Paul Morton: Yes, I think so. Look, there are always the 3 options. The idea of putting money away in a sinking fund or a capital works budget, are] some very obvious attractions. I think the biggest problem with a sinking fund is that people don't stop to think of what are the disadvantages. It's just automatically assumed to be a good thing, and there are some issues with them. Most importantly, there's the cost of a sinking fund and whether you're actually going to get the value for that when you sell your property.

I think the important thing about a sinking fund is what are the pros, but also what are the cons? Special levy, it's a perfectly valid form of financing. The only trouble is that most people in Australia can pull one or two thousand dollars out of somewhere to make a quick payment on a special levy, even if it's unforeseen. But more than about $5,000, and even in the wealthiest suburbs in Australia, there will be people in Australia who have trouble making that payment. Borrowing, it's an option I think should always be considered.

Amanda Farmer: Yes. What are some of the common problems, Paul, that you've noticed people face when it comes to looking at a strata loan and what, in your experience, has worked in terms of overcoming those problems?

Paul Morton: I think the problems about a strata loan are the same as funding in general. Maybe they're the problems of strata altogether. I'd put them into 3 categories. I'd say the first one is naivete. The second once is ignorance, and the next one is emotion. It applies to everything in strata, I think. Naivete, people blindly think that there's only one option, or blindly think that their preferred thing is just the way that everybody ought to go. Now a sinking fund, as I was alluding to before, it's often the most expensive form of funding in strata.

Ignorance. Well, it's just not being aware of the 3 alternatives, or worse, it's not even accepting that you actually need to

consider what mix of those 3 alternatives are going to appropriate in your particular situation at that time. The last one is emotion, and we see this all the time. You would too. "We can't afford it. We don't have any money. Borrowing is bad. Levies are bad. Strata is bad," and people go off on a strange place. I think the solution to that emotional one is to stop thinking about your involvement in strata as being a cost, and start thinking about it as property being a long-term asset.

So everything you do to repair and maintain or improve, or develop, is not an expense, but it's an investment. Now immediately you think about an investment, immediately you're starting to think about return on investment. So it's not an issue of whether we should spend 500,000 or 200,000 dollars, it's what's going to be the best investment for us? How do we get the biggest bang for our buck, for our lifestyle and financially? Because as soon as you start thinking about investment, you must think about return on investment, and that leads you right down the right path, and it takes a lot of emotion out of it. It also helps with the ignorance and naivete.

Amanda Farmer: I really love that take on it, Paul. It's not spending, it's investing, and we should always be looking at how we're adding value. How we're adding value to our property, it's something we talk about on the podcast a lot. That's a real gem there. I can see it's come through your years of experience. I do want to just remind our listeners that you can download the transcript of this episode, and you can bring these gems to your strata committee or your fellow owners, or your strata manager.

You can get the transcript by going to yourstrataproperty.com.au/073, being episode 73. Our listeners, Paul, some of them will have had strata loans before. They'll be listening to you thinking, "Hmm. There are these 3 options. I hadn't really thought about strata loans. It's something I want to explore." What steps do you suggest they take to get started with investigating strata loans today?

Paul Morton: Get on the phone. Call us right now and ask questions direct. Whatever is on your mind about whether it's appropriate or the problems or the hassles, call us and ask, and we'll talk as best we can. We'll also send you a loan proposal, which is something that can be shared around the community, and then we go from that point to a loan contract, et cetera, if that's appropriate. Look on our website, www.lannock.com.au. There's a wealth of information there. Most importantly, talk to your neighbours. But when you're having the conversation with your neighbours, think about that and the reasons why I talked beforehand, remembering there's going to be a lot of naivete, a lot of ignorance and an enormous amount of emotion. You're going to have to work through that, and it will take time.

Amanda Farmer: All good things do. Personal question, Paul. What books have had the greatest impact on you, and why?

Paul Morton: Oh this is like saying who's my best friend, isn't it?

Amanda Farmer: Oh, it's a hard one.

Paul Morton: I think every book has an impact. The thing about a book is it's an invitation. It's like someone knocking on your door, and there's an invitation for you to think about things. As much as I like movies, movies are very controlling things. They invade your head and they say, "Think this, feel this, do this," whereas a book is just a completely different kind of medium. It's an invitation to you. So, therefore, I think that's why it has the impact because you're always engaging with a book, whereas with a movie, you're just being told what to think.

I read a lot of history and it's probably my favourite topic. Little bit of biography and the occasional fiction. Interesting, I just finished a book by Simon Montefiore about the history of the Romanovs, and it's really interesting listening to the current Trump, Russia, Putin-type things, thinking of how Vladimir Putin might act and think in the context of this 300-year or so dynasty of the Romanovs from, what, 1600 and something almost to the First World War. I'm just about to pick up Nicholas Whitlam's Four Weeks that Changed the World, so that's jumping for me. I'm talking several decades into the Second World War.

Amanda Farmer: Well, we'll make sure that we have links in the show notes to those books, Paul, so that our listeners can enjoy them along with you. Now before we wrap up, how do we find out more about you and is there anything you'd like to add before

we say goodbye?

Paul Morton: Call us, email us, Google, talk to your strata manager, talk to other people. Interestingly enough, we get ... at least a third of our inquiries come from owners direct, and usually, that's from word of mouth. It's the dinner party conversation or something like that. The inquiries we get from strata managers, we know quite a lot of them being sort of the catalyst, is an owner saying, "Look, how about we check this out, it's a good idea." So there's a lot of owner power in that, but just to repeat, I think people think money is really ... it's facts and figures, it's about things which are boring, whatever.

Our experience is that money is really, really emotional, and people get really upset really quickly when they're thinking and talking about money, for obvious reasons perhaps. So try and make it objective by asking the question, "What return will I get?" Not, "What does it cost," but "What return will I get? What's the right project for us to undertake," and then, separately, "What's the right mix of sinking funds, special levy and borrowing in this particular case?" That would be my best advice. I think borrowing's always going to be a component of a good plan, but the real thing we want owners to do is to think about the 3 options.

Amanda Farmer: Yes. Very good, clear advice. Thank you so much, Paul. Thanks for your time today and your contribution that you have made over many years in the strata industry, and continue to make. Keep up the good work. I just want to make very clear for our listeners that Lannock is L-A-N-N-O-C-K, and I think you said there Paul lannock.com.au is where you can find out more about Paul and Lannock Strata Finance. Thanks for your time.

Paul Morton: Thanks, Amanda. It was a real pleasure.

Outro: Thank you for listening to Your Strata Property. The podcast which consistently delivers to property owners reliable and accurate information about their strata property. You can access all the information below this episode by the show notes at **www.yourstrataproperty.com.au**. You can also ask questions in the comment section which Amanda will answer in her upcoming episodes. How can Amanda help you today?