

## THE SECTIONAL TITLE INDUSTRY IN SOUTH AFRICA: PERSPECTIVES OF MANAGING AGENTS

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### Abstract

This article is the second in a series of three on the sectional title industry in South Africa. (The first article dealt with perspectives of accounting and auditing practitioners and the third article in the series will address the perspectives of chairmen or bodies corporate.)

The aim of this article was to provide an overview of practical problems experienced by managing agents in the sectional title industry in South Africa by way of interviewing a sample of key role players in the industry.

The empirical results revealed various practical challenges and uncertainties in the industry. Various problems and concerns were addressed and practical recommendations were made that can be of assistance to owners, trustees, managing agents, accountants and auditing professionals. The findings can also be used as a valuable basis for further research.

**Keywords:** Sectional Title, Sectional Titles Act, Sectional Title Management, Sectional Title Schemes, Sectional Title Budget, Trustees, Body Corporate, Trust Money, Accounting, Auditing, Accounting Profession, Auditing Profession

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### 1. Introduction

The research findings in this article form part of the results of an extensive study done on the sectional title industry in South Africa, performed in fulfilment of a Magister degree in Accounting. This article is the second in a series of three articles highlighting the research findings.

The first article in the series sketched the background and overview of the sectional title property industry in South Africa. It also gave a detailed layout of the research methodology and contained a comprehensive literature review. Therefore, these aspects will not be addressed again in detail in this article. This article will commence with the problem statement and aim of the article, followed by the research methodology. A discussion of the empirical findings will then be done under different sub-sections, followed by a conclusion and possible recommendations. The third article in the series will address the perspectives of chairmen or bodies corporate.

### 2. Problem Statement and Aim of the Article

In many cases the trustees lack the time, skill and expertise to fulfil all the functions and duties they are responsible for. Therefore, management rules 26 and 46 of the Sectional Titles Act 95 of 1986 state that the

trustees may appoint a managing agent to be entrusted with various management and administrative duties of the body corporate. Managing agents of sectional title schemes encounter various practical challenges when performing services for sectional title clients. Against this background, the aim of the article is to give an overview of practical problems experienced by managing agents relating to sectional title. Possible solutions recommendations will also be suggested in this regard.

### 3. Research Methodology

The research design was developed to address the research problem stated above. The research consists of a brief literature study, followed by a qualitative empirical study.

Flowing from the literature study, an investigation into current practices and challenges in the sectional title industry was undertaken. A qualitative research strategy was followed and the study was done by way of standardised interviews with sectional title managing agents involved in the sectional title industry limited to the Bloemfontein area in South Africa.

The exact population of the participants was difficult to determine, due to various factors. Many sectional title schemes in Bloemfontein operate without a functioning body corporate and board of trustees and many sectional title schemes operate

without using the services of a managing agent. Furthermore, not all the organisations acting as sectional title managing agents are registered with the National Association of Managing Agents (NAMA) and the Estate Agency Affairs Board (EAAB).

In order to address this practical challenge, the authors undertook extensive consultation among role players in the industry. After the consultation process, a joint decision was made to include five respondents and it was also jointly decided which five respondents were to be chosen. In view of clarity, the decision making process will be briefly discussed.

The five managing agents interviewed were selected after a thorough investigation into the main role players in the sectional title industry in Bloemfontein. The sample was selected to represent two large managing agents (managing more than 100 schemes), two medium-sized agents (managing between 30 and 100 schemes) and one small agent (managing less than 30 schemes). Two of the five managing agents have been operating in Bloemfontein for more than 80 years, one for more than 20 years and the remaining two have been in operation for less than 10 years. The total number of sectional title schemes managed by these five managing agents amount to more than 450.

In order to address the research problem of the article, a research questionnaire was developed as a measurement instrument in order to structure the interviews. The questionnaire was designed to structure the interview process, and ensure consistency of the coverage of questions between the interviewees. A formal cover letter from the authors

explaining the purpose of the interviews and addressing the terms of confidentiality was sent to all interviewees before the interviews. Due to restrictions on the length of articles, the questionnaire was not attached to this article. It is, however, available upon request.

As mentioned in the previous article, various aspects from available literature were taken into account in developing the questionnaires and conducting the interviews.

## 4. Empirical Findings

### 4.1 Introduction

As mentioned above, this section will deal with the results of the information from the questionnaires and interviews with managing agents. These aspects will be discussed under the following headings: clients and services, problems and risks, trustees, training and staff, fees, developers, meetings and financial matters.

### 4.2 Clients And Services

The 5 managing agents interviewed had varying numbers of sectional title schemes as clients, the numbers being 25, 36, 45, 125 and 260 schemes. The managing agents provided a range of services to their clients, which were not all utilised to the same extent. The following figure is a representation of the different service offerings of the managing agents and the percentage of clients making use of the services:

**Fig. 5.1.** Summary of service offerings by managing agents, indicating the percentage of clients utilising the services

	Practitioner				
	A	B	C	D	E
<b>Day-to-day management of the complex</b>	50%	100%	30%	100%	100%
<b>Administrative tasks</b>	100%	100%	90%	100%	100%
<b>Compiling of financial statements</b>	100%	100%	100%	50%	100%
<b>Preparation of budgets</b>	100%	100%	100%	50%	100%
<b>Collection of levies and amounts payable</b>	100%	100%	100%	100%	100%
<b>Assistance with insurance</b>	100%	100%	100%	100%	100%
<b>General maintenance of the complex</b>	60%	70%	80%	90%	100%

### 4.3 Problems and Risks

According to the managing agents, one of the biggest problems experienced with the managing of sectional title schemes is problems with municipal accounts, a frustration shared by accounting practitioners, as discussed in the previous article. Three of the five (60%) managing agents mentioned that account estimates, corrections on statements, incorrect allocations on statements and poor communication and service from local authorities caused countless problems when managing schemes. It also makes it

very difficult to perform analytical procedures on the account balances.

Three of the five (60%) managing agents stated that debt collection is a great challenge. They said that they spend a lot of time and money collecting outstanding amounts, and that the legal processes that have to be followed in the case of non-payment are cumbersome and expensive. One agent mentioned that in the case of tenants, the available deposits are not always sufficient to cover outstanding balances in the case of non-payment.

Three of the five (60%) managing agents stated that uninformed owners and trustees cause many problems when managing schemes. They said that there is a general ignorance among owners and trustees regarding the legislation governing sectional titles. One of the managing agents mentioned that estate agents selling sectional title property are largely to blame, since they do not inform prospective owners of exactly what they are buying into.

One of the managing agents remarked that attracting and retaining competent staff is a great challenge. He said that due to cost constraints, many managing agents cannot afford to employ highly qualified and skilled staff. Another problem that they experience is a high staff turnover, which he attributes to staff members simply using the employment at a managing agent as a stepping stone to another higher paying job.

According to two of the five (40%) managing agents they experience frustrations when registering new schemes with the South African Revenue Service (SARS). They claim that SARS requires large amounts of information and several documents, which they perceive as being very time consuming.

According to three of the five (60%) managing agents, the biggest risk involved in being a managing agent is the fact that, on the one hand bodies corporate give them the freedom to perform the necessary management activities, but on the other hand hold them responsible if they are unhappy with the outcome of the managing agent's decisions or actions. One of the five (20%) managing agents stated that a big risk is the fact that they are only contracted for the first year and thereafter the body corporate can change to a different managing agent with one month's notice. The managing agent stated that this happens quite often. The problem was also raised by accounting and auditing practitioners in the previous article. One of the five (20%) managing agents also stated that they perceived the biggest risk to be taking over a scheme from another managing agent. The managing agent stated that, in the past, they experienced that for such cases it is difficult to verify balances and that the whole process creates various administrative challenges.

#### 4.4 Trustees

The managing agents had varying opinions on whether the trustees of the schemes managed by them are actively involved. Two of the five (40%) managing agents said that they have only actively involved trustees. These two managing agents stated that they have ongoing communication with the trustees and that they go to great lengths to ensure that the trustees are well-informed. Two of the five (40%) managing agents said that 50% of trustees are actively involved, while the other 50% is not involved at all. One managing agent (20%) stated that approximately 25% of the schemes managed by him have actively

involved trustees, 70% have trustees who are not involved at all and approximately 5% do not have any board of trustees.

An observation that was made regarding the above, was that the more schemes the managing agents managed, the less involved they perceived their trustees to be. The managing agents managing the smallest number of schemes all commented that they have fully active trustees.

The managing agents differed in their opinions on what the optimal number would be for a well-functioning board of trustees. One managing agent said more than 3; one said no more than 6; one said 2 to 3 for small schemes and 5 for larger schemes; one said 2 to 5, depending on the size of the scheme; and one said 3 to 5, depending on the size of the scheme.

Two of the five (40%) managing agents stated that, on average the boards of trustees of the schemes managed by them consisted of 5 trustees. One managing agent (20%) said the average is 4 trustees, one (20%) said the average is 3 trustees, and the remaining (20%) agent said the current average is 3 to 5 trustees.

An important observation was that three of the five (60%) managing agents are of the opinion that the average chairman of a board of trustees does not have sufficient skills and knowledge to act as chairman. One of the five (20%) managing agents said that 70% of chairmen are knowledgeable and 30% are not. The remaining (20%) managing agent said that they give formal training to all trustees, and therefore he thinks that the average chairman of a board of trustees has sufficient skills and knowledge to act as chairman. He mentioned that that is only the case for the schemes managed by him, and that he is of opinion that chairmen of other boards of trustees do not have sufficient skills and knowledge to act as chairmen. This problem was also discussed from the viewpoint of auditing and accounting practitioners in the previous article

Five of the five (100%) managing agents remarked that trustees are never compensated for their services. Two of the five (40%) managing agents said that only approximately 10% of the chairmen of boards of trustees receive an honorarium of about R500 per month, and that the rest do not receive any form of compensation. Three of the five (60%) managing agents stated that chairmen of trustees never receive any form of remuneration. One of the managing agents remarked that he thinks trustees and chairmen would take their tasks more seriously if they were remunerated. As mentioned in the previous article, being a trustee of a body corporate is a "thankless" job, and perhaps it may be easier to find individuals willing to serve as trustees if they were remunerated. The fact was also mentioned that bodies corporate should be run like "businesses", and the remuneration of trustees may be a starting point in achieving that. This comment of the managing agent

as well as the other role players should be taken note of by the industry.

Five of the five (100%) managing agents said that if a trustee or chairman made purchases or payments on behalf of the body corporate, they are always reimbursed, provided that they have the necessary invoices.

#### **4.5 Training and Staff**

All of the managing agents interviewed (100%) said that they are entirely up to date with the latest stipulations of the Sectional Titles Act.

All of the managing agents interviewed (100%) said that they give formal sectional-title specific training to all of their newly appointed staff members. Four of the five (80%) managing agents stated that they also give training to current employees, while the remaining managing agent (20%) said that they do not.

Three of the five (60%) managing agents said that there is a need for specialised training courses covering legal aspects, insurance, accounting and the National Credit Act. One of the five (20%) managing agents said that there is no time available to send staff members on training, so they would not be interested in training courses. One of the five (20%) managing agents said that in their business, the areas of work involving more expertise (such as insurance and accounting) are done by outside specialists. Therefore, they have no need for training.

#### **4.6 Fees**

Four of the five (80%) managing agents said that one of the main factors taken into account when determining their management fee is the size of the scheme. All of the managing agents said that they have a general fee per unit, which they use as a guideline. The fee is adjusted up or down depending on a number of variables.

Four of the five (80%) managing agents said that the level of involvement of the trustees also has an impact on their management fee. They stated that they adjust fees upward if the trustees are not actively involved in the management of the scheme.

One managing agent remarked that there should be greater transparency by the managing agents on how their fees are calculated as many trustees complain that they are left in the dark regarding this.

#### **4.7 Developers**

The general viewpoint of the managing agents was that they prefer managing schemes where no developers are involved. The managing agents experienced a number of problems where developers were involved in schemes.

Three of the five (60%) managing agents mentioned that some developers finish building, but leave units without, for example, ceilings, windows or floor tiles. The developer then claims that the units are unoccupiable and refuse to pay levies on those units. The units in the finished section have to subsidise the developer's units with their levies. The managing agents said that this creates budgeting problems and infuriates owners. In some cases the situation is worsened by developers using the water and electricity of the complex during the completion of the building process instead of paying for the water and electricity used by them. One managing agent mentioned that they experienced instances where the developer did not pay the water and electricity bill for the development period and the body corporate had to settle the full outstanding amounts.

Two of the five (40%) managing agents said that developers do not take their role seriously enough in the early phases of the existence of the body corporate. Random sets of management and conduct rules are often registered without taking the interests of the potential future owners into account.

Three of the five (60%) managing agents said it takes a long time (sometimes up to two years) to obtain occupation and electricity certificates from developers. Instances were mentioned where owners wanted to sell their units, and could not do so because of outstanding certificates from developers.

One managing agent also remarked that it happens regularly that developers do not ensure that proper valuation of the scheme is done on completion of every development phase. This creates problems with calculations and budgeting of rates and taxes.

#### **4.8 Meetings**

Four of the five (80%) managing agents stated that in general meetings are poorly attended. All of them stated that 50% to 60% of initial annual general meetings (AGMs) do not have a quorum and have to be postponed. This is despite various communication efforts such as registered mail and sms-messages. Only one (20%) managing agent said that AGMs are well-attended. He attributes the good attendance to the fact that he sends all documents to owners via mail and e-mail beforehand, and sends reminder sms-messages to owners 14 days as well as 7 days before an AGM or other meeting.

One of the biggest problems at AGMs is the approval of budgets. Three of the five (60%) managing agents stated that owners do not understand financial statements and budgets. They remarked that owners do not see increases in perspective and that increases in budgets and the resulting levies are often met with resistance. One of the five (20%) managing agents also stated that at most AGMs, owners want to put impossible cost restrictions on audit fees and management fees. This is a viewpoint that is shared

by accounting and auditing practitioners as well, as discussed in the previous article.

Three of the five (60%) managing agents also said that owners do not adhere to proper meeting procedures during AGMs, and that owners regularly want to discuss operational matters which fall outside the scope of the agenda.

Two of the five (40%) managing agents stated that the election of trustees at the AGM is usually problematic. They said that it is often difficult to find persons willing to serve as trustees, and in some cases trustees are not re-elected, mainly due to past clashes or disagreements with owners.

#### **4.9 Financial Matters**

Four of the five (80%) managing agents stated that the annual financial statements of their clients are prepared by firms of chartered accountants (CA(SA)). The other managing agent (20%) said that the financial statements of approximately 85% of his clients are prepared by a firm of chartered accountants, and the financial statements of the remaining 15% are prepared by a Certified Professional Accountant (CPA).

Five of the five (100%) managing agents said that the audits of financial statements of their clients are done by firms of chartered accountants (CA(SA)).

All of the managing agents (100%) said that the appointment of the auditors is done by the members of the body corporate at the AGM. They stated that they do, however, make recommendations regarding audit firms which give good service in cases when they are asked for advice regarding the appointment of auditors.

All of the managing agents (100%) were of the opinion that cost is the most important factor to take into account when choosing an audit firm. Four of the five (80%) managing agents stated that they also take into account whether the audit firm can deliver the financial statements and audit report on time. One of the five (20%) mentioned that he takes the auditor's knowledge of the Sectional Titles Act into account when choosing an auditor. Only one (20%) managing agent said that the auditor's quality of work is a deciding factor.

Three of the five (60%) managing agents said that they experience bottle-neck situations regarding the receipt of financial statements and audit reports for schemes with February year-ends. They did, however, add that only approximately 25% of their clients have February year-ends. The other two (40%) managing agents remarked that they never experienced any timing problems. This problem was also discussed from the viewpoint of accounting and auditing practitioners in the previous article.

All of the managing agents (100%) were of the opinion that the audit of the financial statements adds value to sectional title schemes; an opinion which agrees with that of accounting and auditing practitioners, as discussed in the previous article. The managing agents stated that an objective opinion on the financial matters of a scheme is imperative. They remarked that it is even more important to perform an audit in cases where a scheme changed from one managing agent to another.

Another budgeting-related matter which was mentioned by three of the five (60%) practitioners is special levies. They were of the opinion that bodies corporate should try to avoid special levies and properly plan and budget for repairs and maintenance and capital projects well in advance. All of the managing agents said that they advise the trustees to build up some form of reserve into the budget every year.

#### **5. Conclusion**

Managing agents encounter various practical challenges and from the results of the interviews with the industry role players, various concerns were identified. Municipal accounts caused serious concerns as well as debt collection. A high staff turnover, pressures on management fees and obtaining budget approval created further problems for managing agents. Some problems with timely receipt of financial statements and audit reports were mentioned. Furthermore, the managing agents had various problems with developer involvement.

In the following article in the series, the perspectives of chairmen of trustees of bodies corporate will be explored.