

## Protecting and Enhancing Your Reputation

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### 1. About this session

- 1.1 This session is about professionalism. If you, as a member of Strata Community Australia, are serious about *“Transitioning from Good to Great”*, then this is a topic that is vital to you and your business.
- 1.2 Professionalism is about many things – commonly related to our academic qualifications, how we dress, how we treat our clients and our peers and the quality of our work. The Merriam-Webster Dictionary defines *“professionalism”* as *“the conduct, aims or qualities that characterize or mark a profession or professional person”*. That definition substantially expands the test of professionalism by introducing the concepts of *“conduct”*, *“aims”* and *“qualities”*. These go far beyond things such as dress, qualifications and work quality. These introduce the concept of ethics.
- 1.3 Ethics are commonly referred to as *“moral philosophy”*, which involves determining right and wrong conduct and practicing the former. Ethics are not something that you can study and then ‘file away’ in your intellectual rag bag. They need to be studied, understood and built into the very fabric of your business. They reflect and enact your values. While laws and Codes can act as guides to ethical behaviour, more is needed. In the long term individuals, businesses and their industry bodies need to focus on instilling integrity.
- 1.4 Ethical behaviour is fundamental to professionalism. If real professionalism is to be achieved it has to be achieved not only at the individual level, but at every level of a business or organization and in every business or organization in the particular field of endeavour. For example, body corporate management will not be perceived as being a professional endeavour unless and until all body corporate management businesses and all persons working in those businesses are themselves professional. Of course, *“all”* is an aspirational expression, but is indicative of the need for professionalism to be perceived throughout the entire field of endeavour.
- 1.5 My focus today will be on ethical behaviour, because that is the fundamental ingredient to professionalism and is the key to protecting and enhancing your reputation both as a member of the body corporate management community and as an individual business. It is also fundamental to Strata Community Australia’s efforts to transition body corporate managers from *“Good to Great”*.

## **2. How do we measure ethical behaviour?**

- 2.1 Behaviour needs to be measured against some identifiable standard to determine whether or not it is ethical. In most professions there are layers of standards, as is the case for body corporate managers. The first and most important set of standards is the management company's "Code of Conduct". This is followed by any legislative code, such as, for body corporate managers, the "*Code of conduct for body corporate managers and service contractors*" in Schedule 2 of the *Body Corporate and Community Management Act 1997* ("**BCCM Act**"). The next and final layer is the Code of Conduct mandated by the industry body of which the business is a member, in the case of body corporate managers, the "*Code of Professional Conduct*" of Strata Community Australia.
- 2.2 Also implicit in ethical behaviour is an obligation to observe the general law of the land – to conduct business in a lawful way. Of course, the law in its broad sense is massive. What is meant by this principle is that one must observe laws relevant to ethical conduct. It does not mean if you exceed the speed limit on your way to work you are acting unethically. Instead, it covers circumstances where relevant Codes may not deal with a specific issue or may deal with it in more detail. For example, engaging in insider trading may not be expressly covered in a Code, but is illegal and unethical.
- 2.3 Sitting with these 3 layers and the general law are community standards, which often progress more rapidly than formal Codes or even the law itself. This also recognizes the commercial reality that clients are ultimately the judge of what is or is not ethical behaviour. This goes to reputation or "brand". Therefore, while one must always be vigilant to observe the standards set by the 3 levels of Codes and relevant law, one must always ensure that higher prevailing community standards are also monitored and observed. It may be no excuse to say "*There is nothing in our Codes of Conduct to say what we have done is wrong*".
- 2.4 The above order of hierarchy demonstrates that the management company's Code is the most important source of ethics. This is because it should embody the standards of any legislative Code, industry Code and the general law, while striving to reach any higher community standards. It follows that the starting point for protecting and enhancing the reputation of your management business is to have a quality corporate Code of Conduct.

## **3. Corporate Codes**

- 3.1 A Corporate Code of Conduct is not an end in itself. They need to be part of an overall ethics program, which I will consider later in this paper.
- 3.2 Simply having a Corporate Code of Conduct and posting it on the staff notice board will not achieve ethical behaviour. Arguably, it may achieve the opposite as it will be perceived as a token attempt to present the organization as ethical. Furthermore, if any breach of a statutory code, industry code or the law is involved it may not help mitigate the situation for the organization. It will not convince the enforcer that the organization is fully committed to ethical behaviour and true professionalism or that the offence is unlikely to occur again.

- 3.3 A Corporate Code of Conduct should be a separate document, identified and promoted as such. It is not sufficient to rely upon conduct rules and procedures that are embedded in policy documents or contracts of employment. It should be an aspirational document which embodies the underlying mission, values and principles of the organization.
- 3.4 A Corporate Code of Conduct would typically have the following contents:
- (a) Introduction
  - (b) Core values of the organization
  - (c) Substantive provisions
  - (d) Information and Resources.
- 3.5 The substantive provisions are the “rules” themselves and they need to embody any legislative or industry codes, either by reference or by replicating their requirements. However, the code should set a standard commensurate with the core values of the organization. Often this will require the corporate code to be much more detailed and stronger than any legislative or industry codes.

#### **4. Legislative Code**

- 4.1 As mentioned, the legislative code applicable to body corporate managers is the “*Code of conduct for body corporate managers and service contractors*” in Schedule 2 of the BCCM Act. That code deals with the following:
- (a) Having a working knowledge and understanding of the BCCM Act
  - (b) Acting with honesty, fairness and professionalism
  - (c) Exercising skill, care and diligence
  - (d) Acting in the body corporate’s best interests
  - (e) Keeping the body corporate informed of developments
  - (f) Ensuring employees comply with the Code and the BCCM Act
  - (g) Not engaging in fraudulent or misleading conduct
  - (h) Not engaging in unconscionable conduct
  - (i) Avoiding conflicts of duty or interest between Schemes
  - (j) Ensuring goods and services are supplied at competitive prices
  - (k) Complying with requests to demonstrate the keeping of particular records.
- 4.2 The Code is not exhaustive of ethical conduct. For example, it is silent on personal conflicts of interest and secret commissions, the former being dealt with under the common law and the latter under the criminal law.

#### **5. Professional Code**

- 5.1 The relevant professional code for body corporate managers is the “*Code of Professional Conduct*” of Strata Community Australia. I understand that Code is currently under review, but at this stage Queensland members are governed by the Queensland version of the code, which is more detailed than the legislative code and imposes the following obligations:

- (a) To be straightforward, honest and sincere
- (b) To be fair and avoid prejudice
- (c) To respect the confidentiality of information
- (d) To work to relevant technical and professional standards
- (e) To maintain an appropriate level of competence
- (f) Not to directly or indirectly pay or accept a secret commission
- (g) To accept the STA's disciplinary procedures
- (h) To comply with rules regarding display of the SCA logo
- (i) To refrain from discreditable conduct
- (j) Not to induce or attempt to induce a breach of a body corporate management contract
- (k) Not to denigrate another member
- (l) To produce and transfer records (including electronic records) when required
- (m) To comply with advertising standards
- (n) To comply with standards and requirements for searches of body corporate records
- (o) To observe certain practice requirements
- (p) To comply with technical standards prescribed by SCA
- (q) To satisfy continuing professional educational requirements.

5.2 SCA members are bound to observe the code through the Constitution of the Queensland organization. A breach of the code can result in disciplinary action being taken against the member. SCA Qld has a detailed process for handling complaints, including complaints regarding breach of the code. Penalties can include suspension and expulsion from membership. In an appropriate case a complaint may be sent on to a regulatory authority, such as the Australian Competition and Consumer Commission.

## 6. Conduct related laws

6.1 There is sometimes an overlap between the general law and the applicable codes. The classic example relates to secret commissions, which are usually prohibited by codes but which also constitute criminal offences. Where this occurs there may be different "elements" to an offence. For example, in relation to secret commissions, Clause 6 of the SCA *"Code of Professional Conduct"* requires a member not to *"directly or indirectly pay or accept a secret commission in any form"*. In contrast, section 442B of *The Criminal Code* (Queensland) provides:

*"Any agent who corruptly receives or solicits from any person for himself or herself or for any other person any valuable consideration—*

- (a) as an inducement or reward for or otherwise on account of doing or forbearing to do, or having done or forborne to do, any act in relation to his or her principal's affairs or business; or*
- (b) the receipt or any expectation of which would in any way tend to influence the agent to show, or to forbear to show, favour or disfavour to any person in relation to his or her principal's affairs or business;*

*commits a crime."*

6.2 There are substantial differences between the 2 requirements. For example; under the code of conduct the "offence" is to pay or accept a secret commission whereas under the Criminal

Code the offence is to “receive or solicit”. Even an unsuccessful attempt to procure a secret commission under the Criminal Code is an offence.

- 6.3 The Criminal Code also contains other secret commission offences and any commission arrangement must be looked at in light of all the relevant provisions, such as:
- (a) Gifts or offers of secret commissions to an agent
  - (b) Secret gifts received by parent, spouse, child, partner, etc. of agent
  - (c) False or misleading receipt or account
  - (d) Secret commission for advice given
  - (e) Offer or solicitation of secret commission in return for advice given or to be given.
- 6.4 It is also important to note that under the *Criminal Code* it is a criminal offence for any director, manager or officer of a company, or any person acting for another, to knowingly take part in **or be in any way privy to** the doing, or the attempt to do, any act or thing without authority which, if authorized, would be in contravention of any of the secret commission provisions (emphasis added). This is an important provision that can be used to advantage when it comes to enforcing the secret commission provisions of a corporate code.
- 6.5 Similar overlaps can occur with regard to “unconscionable conduct”. Unconscionable conduct would be in breach of clause 7 (Ethical Conduct) of the SCA Qld code and it would also be in breach of section 22 of the *Australian Consumer Law* (Schedule 2 Trade Practices Act 1974 (Cwlth)). While the outcomes can be the same, the way in which they are judged and the penalties imposed are vastly different.

## 7. Community standards

- 7.1 It is all very well to have codes and laws, but what are the expectations of our clients? These are important because if we fail to meet them they may choose to take their business elsewhere.
- 7.2 A good example relates to time recording and charges for the so called “Schedule 2” work. Our clients expect us to record our time honestly and fairly so that our charges are reasonable. There is no express provision of any code or criminal law that expressly requires that, although there are a number of provisions that may be breached if one acts fraudulently. The same applies when a body corporate manager generates communications to lot owners simply to generate more disbursements or costs, without proper regard for the need for the communications.
- 7.3 There mere fact that your client cannot point to a particular code of section prohibiting such action does not mean the practice is acceptable. It is circumstances like these where community standards or expectations effectively over-ride all the codes and laws. Doing the right thing, or acting ethically, become the measuring stick.

## 8. High risk areas

8.1 To my mind there are 4 areas of high risk that require particular attention when training staff and managing standards. They are:

- Breach of the fiduciary relationship
- Not acting in the best interests of the body corporate
- Not acting honestly, fairly and professionally
- Secret commissions.

That is not to say that other requirements are unimportant. These are simply the 4 areas that should, in my opinion, be prioritised to ensure an ethical business environment.

### ***Breach of fiduciary relationship***

8.2 The relationship that exists between a body corporate and its body corporate manager is that of principal and agent. A principal and agent relationship is referred to in law as a “fiduciary relationship”. This is a special, very demanding, relationship that requires the agent (i.e. the body corporate manager) to act with the utmost of good faith and to provide undivided loyalty to the principal. This relationship is further enhanced at common law by the fact that the body corporate manager is also a “delegate”, usually of the secretary and treasurer, but sometimes of the committee itself.

8.3 Some of the demands of this relationship include:

- The agent must not put their personal interests before the duty to their principal
- The agent must not profit (in money or in kind) from their position unless the principal has knowledge of the matter and consents
- Consent by the principal must be “informed consent”, voluntarily given (informed consent often requiring disclosure of all relevant circumstances followed by independent legal advice)
- Personal interests and fiduciary duty must not conflict
- One fiduciary duty must not conflict with another fiduciary duty (which mirrors a requirement in clause 9 of the legislative code applying to body corporate managers).

8.4 Examples of breaches:

- Placement of insurance cover in a way that achieves the best commission outcome for the body corporate manager
- Placement of the body corporate’s bank account with a Bank that is providing favourable finance facilities to the body corporate manager
- Favouring a developer owner in relation to a waiver of penalty interest so as to maintain a good relationship with the developer.

### ***Not acting in the best interests of the body corporate***

- 8.5 A body corporate manager may not be acting in the best interests of the body corporate even although they do not receive a personal benefit. For example, if a particular contractor is chosen because of a personal preference of the body corporate manager in circumstances where another contractor would be more beneficial for the body corporate (because of price or otherwise), yet the body corporate manager receives no personal benefit from the choice.
- 8.6 Compliance with this obligation effectively requires the body corporate manager and their staff to apply the following test to all decisions:

*“Is this decision in the best interests of the body corporate? Is there another option that may be more beneficial to the body corporate?”*

### ***Not acting honestly, fairly and professionally***

- 8.7 Clause 2 of the professional code for body corporate managers requires the manager to “*act honestly, fairly and professionally*” in performing their functions under their engagement. This is a very demanding requirement. At the beginning of this paper I dealt with the concept of “professionalism” and its relationship to ethical behaviour. Honesty and fairness is part of what is required for ethical behaviour. Therefore, this clause effectively mandates ethical behaviour in the way in which functions are carried out by a body corporate manager.
- 8.8 Examples of situations that may give rise to unethical behaviour are:
- Withholding information from a committee relevant to a decision being contemplated by the committee
  - Covering up a mistake that has adverse consequences for the body corporate
  - Favouring one faction of owners against another owner, or another faction of owners, in matters relating to a body corporate
  - Doing free or discounted work for a developer in consideration of receiving a management contract for the proposed body corporate. (This is unprofessional in that it aids a breach of fiduciary duty on the part of the developer, the duty being owed to the future body corporate and its future constituent owners.<sup>1</sup>)

### ***Secret commissions***

- 8.9 Express prohibitions on secret commissions are contained in both the SCA Qld Code for members and the Queensland *Criminal Code*. As pointed out above, there are numerous types of secret commission offences, including those for company directors who were complicit in an offence.
- 8.10 The important points to remember are:

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<sup>1</sup> Based on the reasoning in the New South Wales Supreme Court decision in *Community Association DP No. 270180 v Arrow Asset Management Pty Ltd & Ors* [2007] NSWSC 527.

- Soliciting a secret commission without success is an offence
- Any form of inducement or reward (need not be monetary) is a “commission”
- Receiving and offering are both offences
- Diverting the benefit to a parent, spouse or child does not help
- Advice that induces or influences a person to do something that benefits the giver of the advice may also be an offence
- Disclosure will usually avoid an offence, because it takes away the “corrupt” element of the offence (and the level of disclosure is not as high as it is in relation to fiduciary duties).

## 9. Managing ethical standards

9.1 As mentioned earlier in this paper, it is not sufficient to simply have a corporate Code of Conduct in place. There also needs to be a mechanism for enforcement of that code. The type of mechanism will, in a practical sense, depend upon the size of the organization. Typically a medium to large organization may have the following:

- Code of Conduct
- Supporting policies and procedures
- An “Ethics Officer” to monitor the program
- Staff training
- Penalties for unethical behaviour
- Rewards for ethical behaviour
- Periodic review of the Code

9.2 Staff needs to be bound by the corporate Code of Conduct. This can be achieved by incorporating an appropriate provision in their employment contract or by having them sign an actual copy of the Code with a form of agreement endorsed. That agreement needs to be “tied” to the employment contract so that dismissal can be achieved in an appropriate case.

9.3 Supporting policies and procedures typically deal with such things as:

- Appointment and role of an Ethics Officer
- Confidentiality
- Whistle blowing protections
- Manner of handling of complaints
- Adherence to due process
- Available penalties
- Appeals to senior management.

9.3 The Ethics Officer needs to be an independent person who has the respect of both management and the staff. They must be trusted to act fairly and impartially, while being helpful and maintaining confidentiality. They should “steer” the moral conscience of the staff member.



9.4 Staff training is most important and should cover such things as:

- The underlying mission, values and principles of the organization
- The importance of ethical conduct to both the company and the individual staff members
- The corporate Code of Conduct (including content)
- The relationship of that code to the SCA Qld Code and the general law (including content)
- High risk areas
- The role of the Ethics Officer
- Support mechanisms available to staff on ethical matters (including the Ethics Officer)
- The role that clients play in ethical conduct
- The way in which conduct breaches are dealt with
- The penalties that can be applied
- Rewards for good ethical outcomes.

9.5 Some organizations communicate their standards to their clients and suppliers and seek co-operation in maintaining them. This not only looks good but has the potential advantage of clients and consultants actively assisting the ethical process. For example, a large American company involved in a highly regulated industry periodically sends an ethical standards notification to all its consultants. The following is an actual notification (edited for privacy reasons):

Dear Vendors/Suppliers/Lesseees:

As we all know, [REDACTED] is a business existing pursuant to privileged business licenses issued by governmental authorities. Being a licensed business, [REDACTED], and its affiliates, (hereafter collectively "the Company"), is required to conduct itself according to all applicable laws and regulations. In addition, the Company is committed to maintaining high business ethics and standards and all employees are required to conduct themselves in compliance with the published Company's Code of Business Conduct and Ethics.

Specifically, our Company's Gift Policy sets forth that all employees or any members of their immediate families "are prohibited from soliciting gifts, contributions, gratuities, services, or kickbacks from suppliers or customers of the Company regardless of their value." Also, employees or their immediate family members of the Company are "not to give or accept, directly or indirectly, gifts, contributions, or prizes of more than minor value which are in any way connected with the business of, or matters involving, the Company."

For our employees to continue to maintain these standards, we will need your continuing support and cooperation in the future. If any of you or your employees is aware that any of our employees may be behaving or conducting himself or herself in a way that is inconsistent with the expected ethical standard, you may report the potential ethical violation to the Company's Ethics Hotline by dialing [REDACTED] followed by [REDACTED] or through the website: [REDACTED].

Thank you for your understanding and attention to this matter.

Yours sincerely,

## **10. Dealing with breaches**

10.1 Staff and clients need to know that breaches of the various codes and ethical standards will be dealt with. That is why it is important to have proper processes in place and pre-determine the penalties. The process would normally start with a complaint and discovery of a breach. From there the process (in the case of serious breaches) can be along the following lines:

- (a) the staff member would be given a written “show cause” notice:
  - (i) outlining the breach;
  - (ii) setting out the potential penalty; and
  - (iii) requiring them to explain their action and comment on the penalty;
- (b) a meeting would be held between management and the staff member to hear the staff member’s submissions;
- (c) a decision would be made and, in the case of an adverse decision, a penalty would be arrived at, both being notified in writing to the staff member (which would include advice of the effective time of implementation and any right of appeal); and
- (d) at the appropriate time the decision would be implemented.

10.2 Penalties need not always be severe. They may take into account past record, seriousness of the breach and likelihood of it reoccurring. They may range from a reprimand to dismissal. And the benefits of having incentives for good conduct should not be overlooked. Far too often enforcement focuses on penalties when there is substantive evidence that rewarding good conduct can sometimes be more effective than punishing bad conduct.

## **11. Consequences of failure**

11.1 Consequences of failure to have and enforce good ethical standards in our business will depend to a large degree on the type of failure and the circumstances at the time. However, one universal consequence is the potential to adversely impact on the reputation of the organization. Severe reputational damage can occur when a regulatory authority takes action or where criminal proceedings are commenced against the organization or one of its staff. And it should be remembered that reputational damage among staff can be as detrimental as reputational damage among clients. This is because of the effect on the motivation of staff and their perception of the organization that they work for.

11.2 Apart from reputational damage, other consequences may include:

- Termination of a management contract for breach of the legislative Code (because the terms of the Code are taken to be included in the contract – vide section 118 of the BCCM Act)
- Criminal proceedings against the company, a staff member or even a non-participating director for compliancy
- Disciplinary proceedings under the SCA Code, which could lead to expulsion from SCA
- Order to account for profits made on breach of fiduciary duties

- Liability for compensatory damages for breach of fiduciary duties.

11.3 If you are called to account by a Court, a regulator or SCA (or even a body corporate) it will be of assistance to your defence if you can show that you had in place quality ethical standards and appropriate enforcement infrastructure and that the offending conduct was exceptional in light of those safeguards and unlikely to re-occur.

## 12. Take away points

The key take-away points from this paper are:

- Ethical business practices are the key to enhancing your professional reputation
- A comprehensive Code of Conduct for employees, supported by enforcement infrastructure, is the key to establishing and maintaining ethical business practices and thus protecting your professional reputation
- The Code needs to be carefully drafted to take account of any underlying industry code, legislative code, general law and community standards
- Staff needs to be contractually bound by the Code and thoroughly trained in its requirements.

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