

**In Search of Better Ways to  
Govern and Manage Owners Associations**

**Gary Bugden**

Mystrata Pty Ltd

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# **In Search of Better Ways to Govern and Manage Owners Associations**

## **1. Why search?**

- 1.1 Buildings and real estate communities come in all shapes and sizes. They are occupied by all types of people. They comprise a variety of land uses, sometimes mixed within the same complex. Large mixed-use complexes often struggle with a range of design and construction issues – building defects and design defects leading to noise, waste management and other environmental consequences. Some of those complexes also suffer from the effects of poor governance and management structuring – inequitable cost-sharing arrangements and inappropriate governance and management arrangements. Long term caretaking contracts can also be an issue in many of the more complex schemes.
- 1.2 The very size and complexity of some schemes, combined with the variety of problems usually associated with them, makes them difficult to manage within the normal strata management framework. In many cases strata managing agents struggle to meet the expectation of committees and owners, while committee members lack the skill and experience (and sometimes the motivation) to perform to the level required under the current management framework. It is also common for everyone's time to be taken up dealing with issues, often in a reactive way, rather than focusing on the strategic issues confronting the community, including the building of a sense of community and belonging among residents.
- 1.3 Just as Governments the world over have found it difficult, if not impossible, to devise a legal framework that fits all shapes and sizes and all types of people, so too have they found it difficult to come up with a universal system for the governance and management of common interest developments. In some jurisdictions they have not even tried to find solutions. Despite these difficulties there is a pressing need for solutions to be found.
- 1.4 This very diversity and the problems created by it require that the search for improvement continues.

## **2. Governance and management distinguished**

- 2.1 Before continuing, it is important to understand the difference between governance and management. Under the current approach to strata management in Australia the two

are rarely distinguished and both functions are often shared between the committees and the managers, or in many cases, left entirely to the managers.

- 2.2 Governance is akin to a “legislative” function. It involves the setting of policies and objectives, both short and long term. These objectives are sometimes called strategies and this leads to the concepts of “strategic planning” and “strategic decision making”. In the corporate model, this function is carried out by a Board that represents the company shareholders. In an Owners Association context, the committee of the Owners Association is effectively the Board, being the elected body representing lot owners.
- 2.3 Management on the other hand is essentially an “executive” function. It involves implementing the policy and achieving the objectives set by the Board. In the corporate model, the Chief Executive Officer is the person responsible for the implementation process. The Chief Executive Officer is supported by a senior management team and together they discharge the executive functions of the company.
- 2.4 In an Owners Association context, the strata managing agent is akin to the Chief Executive Officer of a company. However, the way in which the two executive officers operate is fundamentally different in practice. This is largely because there is no clear direction in strata and community title legislation as to the precise roles of the Owners Association committee and the strata managing agent. Furthermore, most of this legislation in Australia fails to set up an effective executive model to administer the Owners Association - apart from providing for the appointment of volunteer secretaries and treasurers who have very limited powers and functions. This is particularly so in the case of larger and more complex schemes where it is totally impractical for them to be managed on a voluntary basis.
- 2.5 In summary, in a strata title context, governance involves the setting of policies and strategic objectives for the Owners Association so that it has a clear plan for the future. Management is the delivery of those objectives by means of a pre-determined implementation plan.

### **3. Good corporate governance**

- 3.1 The starting point for good governance is a clear vision for the future. This is best evidenced in a formal Vision Statement. Perhaps the most obvious Vision Statement for an Owners Association is –

*“To manage and maintain the building in a way that enhances real estate values while promoting a sense of well being and belonging among the residents.”*

Although this is clearly a “motherhood” statement, it does provide a direction and focus for the committee and its strata managing agent.

3.2 Once the “vision” has been determined, the strategies and policies to support the vision should follow. Where possible, these strategies and policies should be developed by the committee in consultation with the owners. This would normally involve:

- Deciding on the policies that need to be developed.
- Canvassing the preliminary views of owners (using forums, surveys and more informal lines of communication).
- Developing draft policies.
- Obtaining owner feedback on draft policies.
- Reviewing feedback and finalizing the policies.
- Communicating the policies to owners.
- Enforcing the policies.

The key to developing good and workable policies is communications and owner involvement.

3.3 Other tenets of good governance are:

- (a) committee elections based on clear policies from candidates;
- (b) regular, well structured and open committee meetings;
- (c) committee education and assessment programs; and
- (d) annual reporting against strategic objectives from management to the committee and from the committee to owners.

## **4. Good management**

4.1 In a corporate environment, the relationships surrounding the Chief Executive Officer, the Board and its Chairperson are critical to a successful management operation. The main line of communication is between the Chairperson and the Chief Executive Officer. The Chairperson is available to guide and support the Chief Executive Officer, although the Chief Executive Officer reports directly to the Board. The Chief Executive Officer also assists the Chairperson in setting the agenda for Board meetings, while the Board sets the agenda for general meetings.

- 4.2 Typically, a Board delegates powers and duties to its Chief Executive Officer and members of the senior management team. This management team effectively runs the company within the limits set by the Board's strategies and policies. The team reports regularly, through the Chief Executive Officer, to the Board. A well functioning Board will not become involved in management issues and will leave the running of the company to the Chief Executive Officer and the management team.
- 4.3 In a strata and community title context, the strata managing agent would need to have a good working relationship with the Chairperson and the committee and they would need to work together to set the agenda for meetings of the committee. Because committee members may lack the skills and experience necessary for good governance, strata managing agents may need to be pro-active in promoting good governance and assisting with the development of strategies and policies for an Owners Association. In many cases they may need to "drive" the process, including the development of much of the thinking and supporting materials.
- 4.4 If the corporate approach to management is applied to an Owners Association, the strata managing agent, as executive officer, would:
- Prepare a plan for approval by the committee for the implementation of the strategies and policies determined by the committee ("Implementation Plan").
  - Receive a delegation from the committee of all the powers and functions needed to implement the committee's strategies and policies and to generally run the Owners Association.
  - Progress the Implementation Plan.
  - Report on progress to the committee.
  - Constantly keep strategies, policies and the Implementation Plan itself under review in case changes are required; recommendations for change going from the strata managing agent to the committee.
- 4.4 Of course, in addition to these strategic duties, the strata managing agent would need to ensure that the normal administrative and accounting functions, including regular building maintenance requirements, of the Owners Association are attended to.
- 4.5 With the benefit of a clearer understanding of good corporate governance and management we can now examine how governance and management of Owners Associations progressed in Australia and compare the current practice with a more corporate approach.

## 5. The first generation legislation

- 5.1 The first generation strata legislation in Australia's major jurisdictions did not attempt to come to terms with the practicalities of body corporate governance and management.<sup>1</sup> Provision was made for an elected committee to administer the body corporate, but the underlying assumption appeared to be that the lot owners would undertake the day to day management through volunteer secretaries and treasurers. Committees were not given any strategic focus by their governing legislation.
- 5.2 Professional management emerged from within the accounting profession and real estate agencies, more as a de-facto role rather than as a role formally recognized by the legislation of the day. In the 1960's and early 1970's managers were engaged as contractors with very limited powers, although in many cases they operated in a practical sense as agent of the Owners Association.
- 5.3 It is therefore fair to say that the range of first generation legislation in Australia completely ignored the divided concept of governance and management and assumed that both functions would be carried out by owner volunteers.

## 6. The emerging governance and management model

- 6.1 The first attempt to seriously address the governance and management needs of Owners Associations came in 1973 with the passing of the *Strata Titles Act 1973* by the New South Wales Parliament. That Act:
- Retained the concept of an elected committee as the governing body of an Owners Association.
  - Introduced the position of "strata managing agent" (an executive appointment intended for professional managers).
  - Placed the strata managing agent in a position, viz-a-viz the Owners Association, of a "fiduciary" (thus imposing the somewhat stringent fiduciary duties on the strata managing agent).
  - Allowed an Owners Association to delegate to the strata managing agent the majority of its powers, authorities, duties and functions and the powers, authorities, duties and functions of its chairperson, secretary and treasurer.
  - Recognized, subject to procedural regularities, the acts of the strata managing agent as the acts of the Owners Association.

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<sup>1</sup> See for example the New South Wales *Conveyancing (Strata Titles) Act 1961* and the Queensland *Unit Titles Act 1965*.

- 6.2 While there were some powers, authorities, duties and functions that the Owners Association could not delegate to a strata managing agent (principally being those that were required to be exercised by a special or unanimous resolution at a general meeting), there was a clear ability for an Owners Association to leave all executive administration matters in the hands of the strata managing agent. The scene was then set for a proper corporate governance model to be applied by Owners Associations in New South Wales.
- 6.3 Despite the mechanisms being available, the corporate governance model was never clearly applied in New South Wales after the enactment of that 1973 Act. The reason may be related to the fact that the Act did not actually specify the role of the committee, although the duties and functions of the secretary and treasurer were specified in some detail. The provisions of the Act failed to set up a clear corporate governance regime and although the Act indirectly facilitated such a regime, the professional management industry failed to promote or adopt the corporate model.
- 6.4 The second and third generation legislation in Queensland<sup>2</sup> followed the example set by the 1973 New South Wales Act. Again, although the legislation facilitated the corporate model the professional managers did not promote or adopt that model.
- 6.5 It is interesting to note that the original regulations under the Queensland *Body Corporate and Community Management Act 1997* (the third generation legislation) were subsequently amended to remove the ability of a body corporate (an Owners Association equivalent) to delegate wide powers to a professional manager, except in very limited and difficult circumstances where no committee is in existence. Therefore, the current situation in Queensland substantially restricts the options available for governance and management of Owners Associations and appears to require the committee to effectively be the management arm of the Owners Association.

## **7. Current governance and management practice**

- 7.1 The current governance and management practice for Owners Associations in Australia is relatively uniform, although it does vary slightly according to the jurisdiction and size of the building or community.
- 7.2 Small schemes (2 to 12 lots) are often self-managed. Some have an operational committee with one or two owners taking on the role of secretary and treasurer in a

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<sup>2</sup> The *Building Units and Group Titles Act 1980* and the *Body Corporate and Community Management Act 1997*.



voluntary capacity. Others do not have an operational committee and the burden is left to one or two owners who voluntarily manage the Owners Association, often without too much regard for procedural formalities.

7.3 Many schemes in Australia, believed to be the majority, are professionally managed by strata managing agents. Most of these schemes are thought to have an operational committee comprised of volunteer owners. In simplistic terms, the committee makes the decisions and the strata managing agent implements them. Decisions are usually reactive to particular situations and do not emanate from any set policy or strategy. Many, if not most, of the decisions are management decisions rather than strategic decisions. In a very primitive way this is governance and management in operation. However, it is not good governance and management.

7.4 A recent survey by a strata management company of a very large building managed by that company revealed some interesting information about how that building is being governed and managed. In particular:

- Their longest committee meeting lasted 12 hours.
- The committee meets every 8 weeks.
- Each active committee member spends between 12 and 15 hours per week on Owners Association business.

This example raises a number of questions; whether it is reasonable to expect unit owners to undertake this level of commitment and responsibility; whether some of the issues being dealt with relate to the way in which the building was designed and constructed and the way in which the internal management was set up (some survey answers suggesting that is the case) and whether there is not a better way to govern and manage the Owners Association for that building.

7.5 The governance and management related issues I see with the current Australian situation are these:

- (a) there are motivation issues associated with volunteer committees (committee members are busy and stressed and don't really want to spend much time doing a job that is not appreciated by their fellow owners);
- (b) some committee members focus more on their own interests than on the interests of the Owners Association and owners as a whole (indeed that is the main reason why some are on the committee);
- (c) inadequate skills and experience of committee members often limits the effectiveness of the committee;

- (d) powers are divided between owners and committees in a way (in most jurisdictions) that severely restricts the level of involvement of committees;
- (e) the powers of strata managing agents are (in most jurisdictions) restricted to the extent that they cannot effectively act as a true executive officer of the Owners Association; and
- (f) the current trend in most jurisdictions is to further restrict the roles of the committee and the strata managing agent, driven principally by pressure on Government by minority interest groups (often representing smaller schemes).

7.6 Committee related issues I see are these:

- (a) they generally do not practice good governance (or understand what it is);
- (b) they tend to get too involved in management issues (sometimes out of necessity);
- (c) they do not communicate well with owners; and
- (d) they do not encourage owner participation, particularly on strategic matters.

7.7 Strata managing agent related issues I see are these:

- (a) the strata manager is usually a company and the person who could serve as the corporate “executive officer” (the company employee) is once removed from the chain of command and responsibility;
- (b) the company employee assigned to an Owners Association has their attention divided because of the number of Owners Associations for which they are responsible;
- (c) the operational procedures of many corporate strata managers involve a “departmental approach” to the delivery of services, which can create gaps in information and skills between the management company and the company employee (these gaps being absent from the corporate model where the management team is totally focused on the one “business”);
- (d) few, if any, strata managers provide an “on site” service (which is conducive to higher service levels, including the building of community); and
- (e) the mindset of some strata managers is very much a “record keeping” one with little or no willingness to become involved in the key service area – common property maintenance and enhancement of real estate values – let alone good corporate governance or community building.

7.8 The identification of the above issues is not intended to be critical of strata managers or committees, or even of Government. Also, I make no judgement on the strength of their merits or otherwise. They have been identified simply to demonstrate the difficulties of applying the principles of good corporate style governance and management to an Owners Association, should one wish to do so. They are also relevant in identifying some of the changes that may need to occur if a more corporate style of governance and management is to be applied to Owners Associations.

## 8. Exploring a better governance and management model

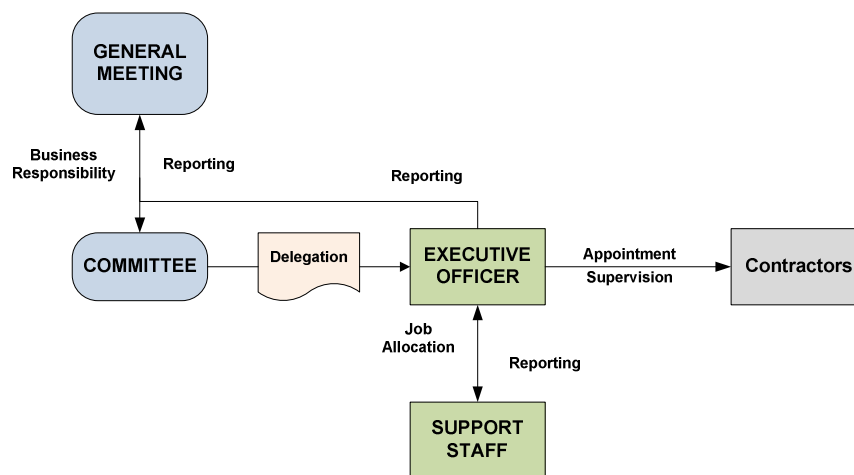
### *What is the best model?*

8.1 The best model must be identified in the context of a particular type of scheme. My concern in this paper is the model most suitable for the more “unusual” schemes, such as:

- (a) very large schemes (e.g. 300 or more lots);
- (b) commercial schemes; and
- (c) schemes with relatively affluent owners and occupiers who are well educated, commercially savvy and demanding.

However, that is not to say that the model would not be suitable for smaller or different schemes. Furthermore, many of the ideas explored in this paper may well have individual application to much smaller, even average size, schemes.

8.2 In essence, the best model is likely to be a strategically focused committee supported by a professional executive officer. The following chart illustrates the model:



### *Role of the committee under this model*

8.3 At the corporate governance level, the committee would:

- Formulate a Vision Statement
- Determine a list of strategic issues and supporting policies that need to be addressed
- Appoint, delegate and supervise a competent Executive Officer (who may be a professional strata managing agent)
- Develop strategies and supporting policies in consultation with the Executive Officer and owners
- Approve the Executive Officer's Implementation Plan for those strategies and policies
- Introduce clear lines of reporting and responsibility
- Conduct regular, well structured and open committee meetings
- Set up good lines of communications with owners (such as a monthly newsletter and community web portal)
- Seek out and make available education programs for committee members
- Introduce annual performance assessment of committee members and the Executive Officer and require the Executive Officer to do the same for any employees and key service providers to the Owners Association.

### *Role of management under this model*

8.4 At the management level, the Executive Officer (or strata managing agent) would:

- Establish good lines of communication between the Chairperson and various committee members.
- Work with the committee to develop the strategic plan for the Owners Association, along with the various policies in support of that plan.
- Prepare and have approved by the committee an Implementation Plan for that strategy.
- Progressively execute the Implementation Plan.
- Set up the administrative structures and arrangements for administration of the Owners Association and the maintenance of its common property and assets.
- Supervise those structures and arrangements.
- Report to regular committee meetings on progress.
- Periodically review the strategic plan and policies and make recommendations to the committee for changes.
- Report annually to the committee and to the annual general meeting.

### *The Strategic Plan*

8.5 A Strategic Plan for an Owners Association would typically deal with the following types of things:

- Vision and Mission
- Review of current status
- Threats and opportunities
- Roles and responsibilities
- Audit and finance
- Risk management
- Corporate governance
- Community building
- Owner and resident communications
- Educational initiatives –
  - Committee members
  - Strata managing agent
  - Owners
  - Residents
- Building and landscape maintenance
- Key Performance Indicators and assessments
- Conflict management
- Review process

### *Owner Association Policies*

8.6 The following are examples of formal policies that may be developed following adoption of a Strategic Plan:

- Investment
- Rules Enforcement
- Levy Arrears
- Reimbursement of Expenditure
- Procurement of Goods and Services
- Dispute Resolution

## 9. Some additional ideas

9.1 Again, focusing on the larger or more sophisticated schemes, the following additional ideas may be worth considering as part of an Owners Associations' governance and management strategy:

- Professional committee members
- Employee strata managers
- Sub-committees
- Wider delegation of functions

Each of these will be briefly considered.

### *Professional committee members*

9.2 This would involve the engagement by the Owners Association of a professional “director” to join its committee, possibly even as it’s Chairperson. This is a universal practice among most public companies and it has the benefit of attracting the special skills and experience needed to gain the best performance from the committee. It is also a common practice among large law, accounting and professional firms. Why would it not be an appropriate practice for particular Owners Associations?

9.3 The benefit of a professional director as a committee member would be to focus the committee and management on the proper way to run a large organization and large budget. It would also ensure that proper corporate governance principles are applied and that appropriate strategies and policies are put in place and implemented. The volunteer members of the committee could learn from the leadership of the professional director.

9.4 A professional director may also assist in the case of an Owners Association that is divided and plagued by internal disputation. They may be able to impartially identify and address the issues underlying the dispute and form a “bridge” between various factions.

### *Employee strata managers*

9.5 Rather than engage a strata management company, a large Owners Association could set up an office on its common property and employ a person to act as its “in-house” strata manager. Affordable web based technology is available in most jurisdictions that will allow a relatively inexpensive office to be established, while

providing the in-house manager with the essential tools required for them to operate outside a large office environment. In the case of very large schemes or schemes with multiple Owners Associations, support staff may also be required, again by way of employment contract.

9.6 This approach is common in North America where many community associations employ their own staff to manage their communities rather than engaging an outside management company. It has the advantage of providing a dedicated on-site presence; the manager being readily accessible to owners and residents. Some of the advantages of in-house on-site management are:

- It provides a higher level of service for owners and residents, delivered at the building or community and not from a remote office.
- It allows for closer supervision of external contractors.
- There is a closer relationship between the manager and the community.
- The manager will have the presence, time and motivation to focus on the building of community.
- It can be more cost effective (depending on the size of the building or community and taking into account the higher service and supervision levels).

### *Sub-committees*

9.7 The formation of sub-committees under the main committee can prove advantageous in larger schemes. Apart from spreading the work-load, sub-committees are an effective way in which to engage owners and residents and extend the line of communications with them. An Owners Association that operates using sub-committees is often more pro-active and productive than one that relies entirely on its committee and strata managing agent.

9.8 If a sub-committee structure is to be used, then special by-laws regulating the constitution and operation of the sub-committees is recommended. These can provide for such things as:

- Membership eligibility
- Charter (i.e. terms of reference)
- Operational procedures
- Funding
- Record keeping and reporting.

9.9 The following are examples of sub-committees that may be considered for a large scheme:

- Finance and Risk Management Committee
- Building and Grounds Maintenance Committee
- Social Committee
- Young Residents Committee

Sometimes there may be the need for more specialized temporary committees, such as a “Building Defects Committee” or a “Refurbishment Committee”.

### *Wider delegation of functions*

9.10 Rather than restricting the duties of the strata managing agent to administrative matters, why not give them a wider delegation of powers and authorities so they can relieve the committee of some of its management burdens and allow it to focus on strategic issues? Clearly, this suggestion will be met with an emotive response from some sectors, in some cases because of previous bad experiences with strata managing agents.

9.11 This suggestion pre-supposes that:

- Clear strategies and policies have been put in place by the committee.
- The strata managing agent chosen is both competent and suitable for the role intended.
- The strata managing agent will report to the committee on a regular basis and will be properly supervised by the committee.

9.12 This suggestion is particularly relevant if a person is employed to act as an in-house strata manager. In those circumstances the manager would be expected to run the Owners Association in accordance with the committee’s strategies and policies and be accountable to the committee or its nominee.

## **10. Legislative change**

10.1 A number of legislative changes would be necessary in most Australian jurisdictions to facilitate the adoption of good corporate style governance and management principles. Changes would also be necessary to facilitate some of the other ideas I have suggested. The type of changes required (or at least desirable) would include:

- Clearer specification of the roles of committees and management.



- Widening of the powers of committees.
- Extension of the powers of Owners Associations to delegate powers and functions to a manager and possibly vesting the power in the committee rather than the general meeting.
- Recognition of an employee manager as an alternative to a professional strata managing agent.
- Recognition of professional company directors as committee members.

10.2 A number of those changes would alarm sectors of the industry, including owners and strata managing agents. The challenge for Government will be to have the courage to act in the face of the likely criticism and out-cry and to identify effective ways to safeguard the interests of those owners who have a genuine concern about abuses of power and process. One way to manage this would be to make the changes for only large schemes and schemes that adopt the model by means of a substantial majority (special resolution or something else short of a unanimous resolution – which barely exists in practice). While this would create a diversified approach to regulation of Owners Associations, the approach is well justified given the huge variety of such Associations that exist today.

10.3 As part of the approach to opening up the roles of the committee and strata managing agents, safeguards can be built in to deal with any abuses that may occur. For example, the process for removal of a committee can be relaxed and powers of veto can be added or strengthened. Also, a general meeting can be given the power to define delegations. The most important outcome is to allow those Owners Associations with a genuine need or desire to avail themselves of a more corporate model of governance and management.

10.4 One model worth considering is the Commercial Regulation Module under Queensland's *Body Corporate and Community Management Act 1997*<sup>3</sup> in the form in which it was originally proclaimed. That Module set up a corporate style of governance and management which, although open to improvement, could potentially work well for larger schemes.

## **11. Financial implications**

11.1 The final matter for consideration is the financial implications for Owners Associations who may choose to adopt a different approach to their corporate governance and management. At the end of the day, any change in approach will need to be costed and compared with the cost of the current approach. It is more

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<sup>3</sup> The *Body Corporate and Community Management (Commercial Module) Regulation, 1997*.

than likely that it will be more expensive because additional time will be involved for the strata managing agent. A value judgment will be necessary to determine if the additional cost is warranted. The one point I would make is that anything which improves the lifestyle of the owners and residents and enhances the value of the owner's real estate will be well worth reasonable additional costs.

- 11.2 Special care needs to be exercised when considering the costs associated with using an in-house strata manager in preference to a management company. While some large schemes could easily bear the cost of an in-house manager and support team without adding to the overall costs of management, the situation will be less clear for others. In those cases the less tangible benefits need to be carefully considered when making a judgment. Reference should be made to the benefits outlined above. Also, it is worth keeping in mind that this is one of the options that can be implemented in all jurisdictions without waiting for changes to legislation.

## **12. Summing up**

- 12.1 There is no easy solution to improving the governance and management of larger Owners Associations. The best starting point would be to move the Owners Association towards the corporate style of governance and try to align its management, as closely as possible, with the corporate style of management. Complete alignment will not be possible until legislative change occurs, although New South Wales Owners Associations have more opportunity to progress in this direction than those in other States because of the more liberal rights of delegation that exist in New South Wales.
- 12.2 Larger and more complex Owners Associations need a new model to help them cope with the challenges they face. Governments need to focus more on these needs and the Associations themselves, along with their industry groups, need to open or progress discussions with Governments to make them more aware of the issues confronting large and complex projects. Governments need to come to terms with those issues and seriously consider introducing a special governance and management regime for large schemes and for those special schemes that can operate more efficiently in a substantially deregulated environment.
- 12.3 Some of the issues confronting Owners Associations for large and more complex buildings and communities relate to design and construction issues and issues caused by the way in which the operational and management arrangements are established by the developer. Governments need to explore these issues and consider ways in which these large and complex projects can be made easier to manage. This may require changes to building standards, more attention to quality control in the

construction process, more attention to the design and operation of mixed use complexes and greater supervision over how developers structure the management arrangements that are “inherited” by the Owners Association.

- 12.4 In the meantime, there are measures that larger and more complex Owners Associations can take without waiting for legislative change. They can start to move towards a corporate model of governance and management, open or improve lines of communications with owners (and residents), establish a system of sub-committees and consider the possibility of an in-house on-site executive officer.

**Gary Bugden**  
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