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MACQUARIE University
SYDNEY · AUSTRALIA

18 December 2023

Embedded Networks
Independent Pricing and Regulatory Tribunal
PO Box K35 Haymarket Post Shop,
Sydney NSW 1240

Dear IPART,

Re: Submission to Embedded Networks Draft Report December 2023

This submission should be read in conjunction with the attached draft paper "Green Strata: Just transition to green energy in housing development". That paper was written as part of my ongoing research on embedded networks in strata schemes, which is part of my larger research on strata title. I am the author of *Strata Title Property Rights: Private governance of multi-owned properties* (Routledge 2017), as well as multiple academic articles in the area. I have been engaged by governments in Australia and overseas to advise on their laws in relation to high density development. I am a long-term Academic Fellow of the Australasian College of Strata Lawyers, the peak industry body for lawyers working in strata industry. I am not an expert on energy regulation and have tried to focus my submission on aspects of embedded networks that relate to high density housing, my area of expertise.

I note that I am not a stakeholder in either the strata or energy industry. I am a professor in a publicly funded university, employed to produce objective, informed research for the benefit of the Australian community.

I will start my submission with some foundational principles that should guide regulatory reform in this area, followed by specific responses to the IPART draft report.

Foundational principles

1. *Strata title*

One of my primary concerns in relation to the multiple government reviews that have been conducted on embedded networks is that while they have included excellent energy regulation expertise, from government, industry and stakeholders, they have included very little legal expertise in relation multi-owned properties, in particular strata title. Embedded networks only exist where there is a group of consumers who create the opportunity to bulk purchase

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energy or water. Those consumers do not exist in the ordinary freestanding housing market; they only exist in properties with multiple owners, that is, in strata and community title, retirement villages (which are often strata title), land lease communities and shopping centres. The legal structure of multi-owned properties is fundamental to any consideration of embedded networks, because the problems that have emerged with them are simply another example in long line of problems connected to developer-made contracts, stretching back to the 1960s, in Australia and overseas (see paper attached). Problems with embedded networks cannot be solved unless energy regulation is viewed in context; in this case, the context is the legal structure of multi-owned housing.

2. *Housing is not an optional consumer item*

When people acquire housing, by purchase or lease, they are not 'consumers' shopping in a market for an optional product, like a TV or car. If consumers of TVs or cars do not like what the market has to offer, they can acquire nothing. That is not the case with housing:- homelessness is not an option anyone would voluntarily choose. As a result, all people who buy or lease housing do so in circumstances in which they *must* agree to something the market offers, whether they like its terms or not.

The more consistent the market product, for example strata title apartments with standard by-laws, similar facilities or embedded networks, the less 'choice' people have. Given the notoriously expensive nature of the Australian housing market, both for purchase and leasing, many people have no choice but to take whatever housing they can afford. As a result, it is imperative that governments ensure that housing and the essential services that people use in their housing, (energy, water, sewerage etc) are only offered on a fair and equitable basis. There is nothing revolutionary in this concept. For example, the reason Australia does not generally have slum housing, unlike many other countries, is because we have legislation (residential tenancies Acts) that sets a baseline standard below which landlords may not offer property to the market. They must meet that standard, no matter how much they insist they are not able to do so and no matter how profitable it might be for them to do otherwise. The same principles should apply to all other parties involved in the housing market; that is, it does not matter how profitable it may be for them create particular legal structures for housing, if those structures fall below a baseline standard of fairness and equity, they should be prohibited.

3. *Strata title apartment buildings belong to their collective owners*

Strata titles are created by the *Strata Schemes Development Act 2015* (SSDA) and regulated by the *Strata Schemes Management Act 2015* (SSMA). These Acts are designed to allow for the collective ownership and management of apartment buildings by citizens. The SSDA subdivides land and air into individually owned apartments and common property. When people buy an apartment, they purchase a legal fee simple (just like a freestanding house) which is coupled with a proportionate share of common property, which includes all

infrastructure. The SSDA automatically creates a body corporate, which in NSW is called an owners corporation (or community or neighbourhood association in community title developments[1]). Bodies corporate are made up of all owners, not tenants, (who unfortunately have little to no say in the buildings they call home). While bodies corporate may be assisted by a smaller strata committee and/or engage a strata manager, they remain the ultimate authority in all schemes; they exist so that people can manage their building and community.

In the context of embedded networks, the capacity to make savings from a discount on the bulk purchase of energy comes from the existence of a collective group of owners and tenants. *As a result, that discount belongs to the owners and tenants*. It does not belong to the developer, who does not have a right to effectively sell that discount to a third party embedded network operator (see paper attached). Nor does the developer have the right to sell the infrastructure to a third-party operator or create contractual rights over that infrastructure in favour of a third-party operator. Apartment owners pay for infrastructure when they purchase their apartments, along with their proportionate share of common property. To the extent that developers are effectively able to sell the discount and rights to infrastructure through contracts that bind owners corporations, this is an abuse of the strata title legal form. Owners corporations do not exist for developers to make additional money on developments, and they do not exist so that third party operators can benefit from long term contracts.

4. *Embedded networks: third party operators v owners corporations*

Much of the existing regulation of embedded networks, such as AER exemptions, seems to be based on an assumption that embedded networks are being operated by owners corporations. Some no doubt are, although these do not seem to have figured prominently in submissions to any government reviews. The only embedded networks that seem to be the subject of consumer complaint, and thus the driver for much government investigation, are embedded networks run by third parties. This may be because there are many more third party operator networks or because they are the only networks with unfair terms. Whatever the reason, it is clear that government regulation needs to be able to distinguish between embedded networks genuinely run by the owners of the building (the owners corporation), who along with their tenants, pay the bills, and embedded networks run by third party companies. Owner corporations in strata schemes and community or neighbourhood associations in community title schemes are all identifiable by their plan numbers e.g., 'The Owners' - Strata Plan No 58068 or Community Association DP No 270180.

<u>Responses to IPART Draft Report</u>

5. The draft report noted at p 23 that 'For non-embedded network customers, only the cost of energy is recovered through retail energy prices. The other costs are incurred

[1] These are low rise schemes that use the same legal structure as strata title. They are created under the Community Land Development Act 2021 (NSW) and the Community Land Management Act 2021 (NSW).

upfront, initially by the builder and recovered through the sale of the property, or by the owner of the property. Several stakeholders indicated that for embedded networks, customers should pay a share of the cost of the embedded network operator's investment in the infrastructure required.'

This seems to indicate a misconception about how upfront costs are borne in relation to embedded networks. Apartment purchasers pay for the cost of the energy and water infrastructure in exactly the same way that other property owners do. Developers do not discount apartment sales because the developer did not pay for the infrastructure; developers charge purchasers as much as the market will bear for apartments. Legally, when people buy an apartment, they acquire a legal fee simple to an apartment, coupled with a proportionate share of the common property on which all infrastructure is sited. Any infrastructure which is attached to the land is a fixture, making it part of the common property, irrespective of contracts to the contrary.[2] The developer not paying for infrastructure is a windfall or kickback voluntarily provided by embedded network operators in return for causing the owners corporation to enter into a long-term contract with the embedded network operator. By insisting that 'customers should pay a share of the cost of the embedded network operator's investment in the infrastructure' operators are in effect suggesting that apartment owners should pay for the infrastructure twice – once to the developer pursuant to their sales contracts, and then again to the operator pursuant to a developer-negotiated contract between the operator and the body corporate. Operators being 'deterred from providing the current level of investment' simply means that it would no longer be financially worthwhile for them to install infrastructure in developments for free. Given the damning evidence of consumers' experience of embedded networks, presented to multiple Parliamentary inquiries (see paper attached), this would seem a positive development.

At p 24 the draft report states that 'Where the total costs of providing an embedded network (energy plus internal infrastructure) exceed the costs that can be recovered through regulated prices, it is appropriate for owners corporations to incur the internal infrastructure costs, because they are better able to manage these costs'.

It is not entirely clear what this suggestion means and how owners corporations should incur the internal infrastructure costs. Does IPART mean through contracts with the embedded network operator? If so, please refer to the paper attached. Those contracts will rarely, if ever, be fairly negotiated for the owners corporation, i.e., the collective consumers. Also, note that the owners (who make up the owners corporation) have all individually already paid for the infrastructure when they bought their apartments, as noted above.

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[2] *SPIC Pacific Hydro Pty Ltd v Chief Commissioner of State Revenue (NSW)* [2021] NSWSC 395; (2021) 113 ATR 24

When it comes to the ongoing costs of maintaining that infrastructure, the owners corporation has a statutory obligation to do so under the *Strata Schemes Management Act 2015* (NSW), s 106. That statutory obligation and liability exists irrespective of any body corporate contracts in relation to infrastructure. Of course, the body corporate could engage a third party provider to do the necessary work for the owners corporation to comply with its statutory obligations, but that engagement should be negotiated by the owners corporation independently of the developer. Given the fact that owners corporations are made up of an ever-changing group of people, those contracts need to be renegotiated on a regular basis so that they represent the agreement of the current owners of the building and its infrastructure. Any business models created by third parties who want to provide services to owners corporations must be able to function in the real-world context of apartments – they are housing owned by multiple private citizens who have the legal and democratic right to determine who services their property. If the embedded network business model is dependent on customers (owners and tenants) being tied into long term contracts by another party (the developer) it is a poor business model that should not be supported by regulation.

The draft report goes on to say, 'Ensuring that the parties who can manage the risks face the costs provides a much greater incentive for them to ensure that services are provided efficiently. To the extent that this drives greater engagement in the market, this should help increase competition and reduce the costs of embedded network services.'

Again, it is not entirely clear what IPART means by this statement (and apologies if that is a failing of understanding on my part), but to the extent that it is a suggestion that embedded network operators engage in a genuine market process of offering their services to owners corporations, I would support this. Instead of the current developer-installed model of embedded network operators, it would be preferable if Australia developed an industry that provides services directly to bodies corporate to manage body corporate owned energy infrastructure on a fee for service basis. That is what we will need if 45% of Australia's energy is going to come from privately owned DER by 2050, as anticipated (see paper attached). Just as non-strata property owners need electricians, plumbers, solar panel companies, lawyers, builders, and real estate agents to help manage their homes, so too do bodies corporate. The size of many apartment buildings means that the infrastructure will be more sophisticated and the provision of services potentially more profitable, but that does not justify companies being installed in buildings by developers, leaving owners and tenants with no choice about who manages their infrastructure and provides them with energy.

6. The draft report states at p 34 that, 'Contributions are provided in exchange for the establishment of a contract with the owners corporation that is then executed at the inaugural annual general meeting. These contributions are then recovered from the embedded network customers over the life of the contract. Capital contributions may be relatively large to secure the contract with the developer and often lead to situations where the owners corporation does not own the embedded network infrastructure'.

   It is not clear that IPART is aware of quite how problematic these developer-made contracts are. Contracts are invariably negotiated primarily in the interests of the parties who negotiated them, that is the developer and the embedded network operator. Contracts like this have caused considerable dispute in strata and community schemes in Australia over the past three decades, and globally, in the past half century. Contracts have related to a range of services imposed on bodies corporate by developers, including strata management, building management, security, landscaping, telecommunications, water, sewerage and energy. Taxpayers have incurred considerable expense paying for government reviews and legislative reform to minimise the damaging effects of these contracts. The current IPART review, along with the AER review, and multiple parliamentary inquiries into embedded networks, are all cases in point. For a fuller explanation of these contracts, please see paper attached. For a shorter explanation, see Professor Cathy Sherry, 'Minns must stop this energy rort before development binge' *Sydney Morning Herald*, 14 November 2023.

   It is important to note that, in New South Wales, the sale of contracts by developers has been held to be a breach of a fiduciary duty owed by a developer to an owners corporation, leading to developers being required to disgorge any profit they have made: *Community Assoc DP No 270180 v. Arrow Asset Management Pty Ltd* [2007] NSWSC 527, [229] (McDougall J). People who knowingly participate in breach of fiduciary duty, such as embedded network operators, are also potentially liable under the rule in *Barnes v Addy* (1874) LR 9 Ch App 244, and could be made to hold contract or property rights they have to infrastructure on constructive trust for the person to whom the duty is owed (the owners corporation). Further, anything that is attached to land, like embedded network infrastructure, is a fixture, that belongs to the landowner (the owners corporation), *irrespective* of contractual agreements to the contrary: *SPIC Pacific Hydro Pty Ltd v Chief Commissioner of State Revenue (NSW)* [2021] NSWSC 395; (2021) 113 ATR 24.

7. *Split incentives*

   I note that the example used by IPART at p 36 is the retrofitting of an existing apartment building. It may be that it is economically efficient for the owners of an existing building to bring in an embedded network operator. That is their decision. However, that is fundamentally different to the embedded networks that have been the

cause of consumer complaint, that is, those that are created by developers and effectively imposed on purchasers.

When it comes to the economics of sustainability infrastructure, there is no doubt that allowing an embedded network operator to install infrastructure in a building for free creates a market incentive for developers to build sustainability infrastructure. But so too would allowing third parties to install energy efficient white goods and lighting, sustainably manufactured tiles, carpet, paint, roofs, windows, balustrades etc. There is no end to the elements of a building that a developer could allow a third party to install for free, with the third party recouping their costs and earning on-going income from a contract with an owners corporation. Developers cannot do this in non-strata housing because of the century's old, rational prohibition on positive obligations (i.e., to pay money) on freehold land (see paper attached). It is not legally permissible for a developer to sell an ordinary house and make the purchaser and successive owners pay a third party, such as a solar or air conditioning company, for infrastructure or services. The only reason it is legally possible in strata title is because of the existence of a separate body corporate that can be bound by contracts, which successive apartment owners have to pay, and because of the levying provisions in strata legislation. *However, the body corporate and levying provisions were not created for this reason.* They were created so that private citizens could manage their collectively owned buildings. Use of these legal forms to bind owners to long term contracts that benefit third party service providers is an abuse of the strata title legal form.

Ultimately, the best way to ensure that sustainability infrastructure is included in new development is to mandate it as a condition of development consent, (while simultaneously prohibiting the developer from binding the owners corporation to third party contracts). As above, there is nothing revolutionary about this. Mandating that developers build in specific ways, that protect or further the community's interests (e.g., in accordance with the National Construction Code; including the provision of open, green space etc) is an inherent feature of development that always needs to be accounted for in the costs of projects.

Finally, it should be noted that the 'innovation' that some participants claim that the current market fosters is often not innovation at all. It nothing more than developers identifying new ways to make profit at the expense of bodies corporate through long used contractual means. It might seem 'innovative' to new players in the energy market; to people in the strata industry, it is more akin to Groundhog Day.

8. *Detailed proposals on pricing methods for gas, electricity, hot and chilled water*

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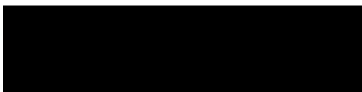
In relation to the detailed proposals IPART has made on pricing gas, electricity, hot and chilled water, I support the proposals that provide the highest level of protection to customers. While IPART has no direct authority for the legal structures that govern strata and community title, retirement villages or land lease communities, it is essential that energy pricing is understood in the context of these legal structures. As noted at the beginning of the submission, the only reason that savings and thus profit are available for embedded network operators is because of the existence of a group of consumers. Those savings should belong to those consumers, not third party companies that have inserted themselves between customers and retailers. Third party companies should be encouraged to develop businesses that provide expertise directly to owners corporations on a fee for service basis. Third party service providers should not be relying on developer-negotiated contracts which they pay for in kind, constituting a significant upfront cost to starting their businesses. Ultimately, the only party that benefits from this system is the developer.

Conclusion

We are on the brink of an avalanche of renewable energy infrastructure as we strive to reach net zero by 2050. Much of this infrastructure will be installed in high density and master planned housing, which will increasingly be home to millions of Australians. Australia needs renewable energy infrastructure, but not provided through business models that harm a particular group of consumers. The Australian housing market is already deeply inequitable without adding exploitative energy contracts to the mix. I would recommend any reform options that provide the maximum protection to citizens (consumers), even if they have adverse effects for third party businesses or developers. This will produce the most sustainable systems, both environmentally and socially, for the nation.

I commend IPART on the detailed work it has done on this complex issue.

Yours sincerely,



Professor Cathy Sherry

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Green strata: Just transition to green energy in housing development

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The 2017 Final Report of the Electricity Network Transformation Roadmap estimated that by 2050 up to 45% of Australia's electricity supply could be provided by millions of privately owned renewable energy generators, storage and management systems.[1] Known as 'distributed energy resources' or DER, these privately owned systems are any renewable energy unit that produces and/or manages power at household or business level. The most common examples are rooftop solar PV units, battery storage, thermal energy storage, electric vehicles and chargers, smart meters, and home energy management technology.[2] Rather than sourcing their power from the grid, millions of Australians will be producing or managing their own power, 'behind the meter' at household level. With the exception of electric vehicles, which are chattels, almost all other DER will be attached to land, making them fixtures (irrespective of contractual agreements to the contrary) and the property of the person or entity that owns the land.[3] As a result, private property law, both common law and statutory regimes, will be a fundamental part of the regulatory framework of DER.

Looking at the residential housing market in Australia, where much of this DER will be located, the majority of Australian households still live in freestanding, freehold fee simple homes, in other words, the iconic Australian dream. However, as a result of

[1] CSIRO and Energy Networks Australia 2017, *Electricity Network Transformation Roadmap: Final Report*, 2.

[2] Australian Renewable Energy Agency, 'Distributed energy resources', https://arena.gov.au/renewable-energy/distributed-energy-resources/, accessed 12 October 2023.

[3] *TEC Desert Pty Ltd v Commissioner of State Revenue (Western Australia)* (2010) 241 CLR 576; *SPIC Pacific Hydro Pty Ltd v Chief Commissioner of State Revenue (NSW)* [2021] NSWSC 395; (2021) 113 ATR 24.

consistent state urban consolidation policies,[4] increasing numbers of people live in strata title apartments. In New South Wales, there are just over 1 million strata apartments that are home to almost 1.3 million people or 16% of the population.[5] Although strata title has existed since the early 1960s,[6] 43% of NSW strata schemes were created after 2000. With the current Minns government enthusiasm for high density development, that figure is set to rise sharply in coming years. In Victoria, half a million people (8% of the population) live in almost 1 million strata lots, with 55% of schemes registered since 2000. In Queensland, 400,000 people (8% of the population) live in 500,000 strata lots, with half being built after 2000. In the remaining states the number of strata schemes is smaller, but growing, as all cities seek to minimize urban sprawl. These figures are an underestimation of the real numbers of strata residents as they do not capture low rise developments, often called 'community title'.[7] These developments are master planned estates that use the same legal structure as strata title. Individual lots will be townhouses, freestanding houses, or even initially vacant land, rather than an apartment. These developments range from coastal golf course housing estates[8] to rural intentional communities or communes.[9]

Strata schemes are not simply home to millions of people, they constitute big business. First, almost 50% of apartments are owned by investors, who as a result of federal

[4] Hazel Easthope, Bill Randolph and Sarah Judd, 'Governing the Compact City: the Role and Effectiveness of Strata Management' (CityFutures Research Centre, 2012) 10.

[5] All figures come from UNSW City Futures*, Australasian Strata Insights Report and Infographics,* 2022.

[6] *Conveyancing (Strata Titles) Act 1961* (NSW). Most states enacted similar legislation in the 1960s, which has been reformed at least once. The NSW strata legislation has been reformed three times, in 1973, 1996 and 2015. The current legislation in NSW is the *Strata Schemes Development Act 2015* (NSW), which deals with the subdivision of land, and the *Strata Schemes Management Act 2015* (NSW), which regulates the on-going operation of schemes. The basic structure of all states' strata legislation is the same, and to avoid the inclusion of multiple similar provisions, this chapter will use the NSW legislation as the exemplar Acts.

[7] Queensland uses the term body corporate community for high and low rise estates created under the *Body Corporate and Community Management Act 1997* (Qld), but most states use the term 'community title' for low rise subdivisions. In NSW, community title estates are created by the *Community Land Development Act 2021* (NSW) and regulated by the *Community Land Management Act 2021* (NSW).

[8] For example, Magenta Shores on the NSW Central Coast, https://magentagolf.com.au/play/ and Sanctuary Cove on the Gold Coast, Qld, https://sanctuarycove.com/, accessed 25 October 2023.

[9] For example, Crystal Waters Ecovillage on the Sunshine Coast, Qld, https://crystalwaters.org.au/, accessed 25 October 2023

government tax policies, such as negative gearing and the partial capital gains tax exemption, have been encouraged to treat residential property as an asset class for building wealth.[10] Then there are the businesses that service strata schemes – strata management agencies, building managers, real estate agents, lawyers, and tradespeople. In 2021, the total value of professional services provided to strata schemes in Australia was over $650 million, and the total value of trades services over $6.9 billion. Finally, there are businesses *physically embedded* in strata schemes by developers. These are the owners of infrastructure such as a hotel, serviced apartments, a rental manager's office, grey and blackwater treatment plants and increasingly DER, coupled with contracts that bind the bodies corporate. The value of these businesses is unknown and growing.

<u>What makes strata property rights attractive for DER?</u>

It is the legal structure of strata and community schemes that make them attractive for DER and other infrastructure. Whether high or low rise, all schemes are created by the registration of plans of subdivision that divide land into individually owned lots – apartments, houses, vacant lots – and common property. Common property is typically the corridors, stairs, foyers, lifts, and car parks of an apartment building, and possibly recreational facilities like gyms and pools. In community schemes, the common property will be more extensive - roads, pavements, parks, bushland, stormwater and sewerage – in other words, infrastructure that is traditionally publicly owned. Whether in a strata or community scheme, all common property is owned by lot owners as

[10] Isla Pawson, 'Reframing Australia's housing affordability problem: The politics and economics of negative gearing [2018] *Journal of Australian Political Economy*, (81), 121–143.

tenants in common,[11] in proportion to their lot or unit entitlements.[12] Contrary to lay assumptions, even if publicly accessible, common property is private property.[13]

Common property is the first attribute of strata and community title that facilitates the provision of green infrastructure, including DER. As noted above, plant and equipment, such as solar arrays, batteries, or meters, must be physically located on some land, and as a result of the doctrine of fixtures will belong to the landowner. Because strata title allows for the collective ownership of land – common property – it also allows for the collective ownership and use of DER, if DER are located on common property. Instead of everyone owning their own individual solar panels or batteries, owners in a strata or community scheme can collectively own DER, including more substantial and technologically sophisticated DER than they could afford alone.

Second, unlike ordinary houses that we can allow to fall down around our ears, strata schemes have a statutory obligation to maintain and repair common property.[14] This is the fairest option for collectively owned land and buildings, because if left to their own devices, some owners would fail to pay for maintenance and repair. Each year, the scheme must estimate its administrative and capital works costs and levy individual owners accordingly.

While this might seem obvious, it is in fact revolutionary in orthodox property law, and was the single most important driver for the initial enactment of strata title legislation. This is because in orthodox Anglo-Australian property law, while it is possible to sell a

[11] There are only two ways to own property with others in Anglo-Australian law – as joint tenants or tenants in common. Joint tenants own in equal shares and if one dies, the other takes the property by survivorship. It is the appropriate form of co-ownerships for spouses. In contrast, tenants in common can own in unequal shares, and there is no right of survivorship. It is the appropriate form of co-ownership for commercial parties and for unrelated lot owners in a strata scheme. The term ‘tenant’ can be misleading; in this context, it simply means owner and does not indicate the existence of a lease.

[12] All lots in strata schemes have a ‘unit entitlement’. The total unit entitlement for a scheme is a random number, for example, 1000, but the number allocated to a specific unit, for example 70 or 96, represents the unimproved market value of a lot relative to other lots. For example, a three-bedroom penthouse might have a unit entitlement of 110, while a studio apartment has a unit entitlement of 60. Unit entitlements determine an owner’s share of the land should the scheme ever be terminated, and the land sold. They also determine the owner’s share of the overall levies that must be paid each year to run and maintain the scheme.

[13] Cathy Sherry, ‘Does Discrimination Law Apply to Residential Strata Schemes?’ (2020) 43(1) *University of New South Wales Law Journal* 307, 311-312.

[14] *Strata Schemes Management Act 2015* (NSW), s106.

freehold fee simple coupled with a restriction (e.g., not to build above a certain height, not to subdivide, not to use the premises for commercial use),[15] it is not possible to sell a freehold fee simple coupled with a positive obligation to pay money.[16] There is good reason for this. Feudalism had acquainted generations of judges with the problems associated with landownership burdened by feudal 'dues' (monetary payments). Judges and parliaments worked for centuries to eradicate property doctrines that allowed feudal overlords and long dead ancestors to impose obligations and control over current owners' use of land.[17] The product of this was the modern freehold fee simple, the most fulsome and free interest in land, that allows the current owner to socially and economically exploit that land as they please, subject only to government regulation. This freedom is simultaneously a product of, and constitutive of, capitalism and democracy.[18] However, if a high rise building or master planned estate is going to be subdivided into individual freehold fees simple – the political preference of successive Australian governments and electorates[19] - the prohibition on positive obligations on freehold land must be overcome to ensure the collectively owned common property is maintained. That is what the levying provisions in strata title legislation do: they impose positive obligations to pay money on freehold fees simple.

Desirable as this may be, the consequence of circumventing the prohibition on positive obligations means that developers are now free to sell fee simple titles and impose obligations on them to pay not just for the maintenance of a building, but for an unlimited range of infrastructure and facilities. That is why we have lifestyle or resort style master planned estates today, with private pools, gyms, landscaped gardens, and sporting facilities, and we did not have them in the past, specifically, any date prior to the enactment the *Sanctuary Cove Resort Act 1985* (Qld), the first legislation to facilitate this kind of development.[20] Net zero targets now mean that infrastructure is

[15] These are *Tulk v. Moxhay* (1848) 2 Ph 774; 41 ER 1143 restrictive covenants.

[16] *Austerberry v. Corporation of Oldham* (1885) 29 Ch D 750 (CA); *Pirie v. Registrar General* (1962) 109 CLR 619.

[17] A W B Simpson, *A History of the Land Law* (Clarendon Press, 2nd ed, 1986), 208-9.

[18] Joseph William Singer, 'Democratic estates: property law in a free and democratic society', [2009] 94(4) *Cornell Law Review* 1009.

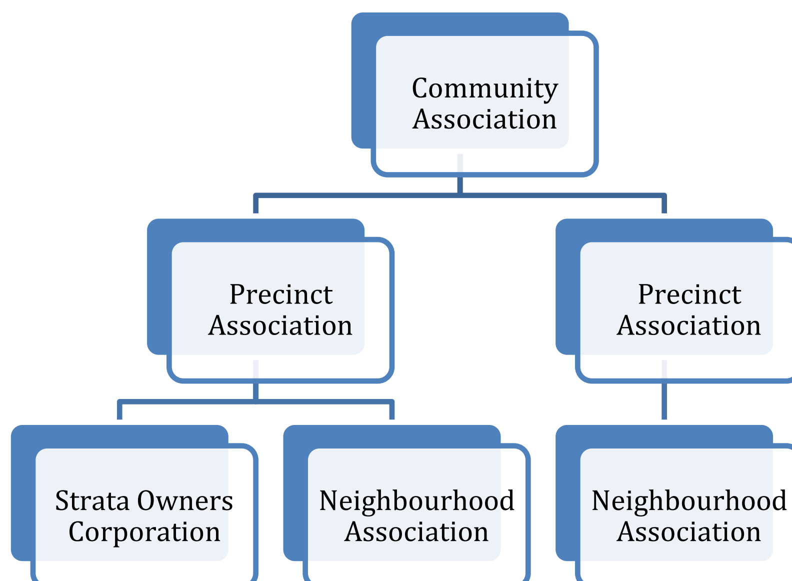
[19] While long term leasehold is the norm in many jurisdictions, Australian governments and citizens have a centuries' old preference for freehold fees simple: Cathy Sherry, *Strata Title Property Rights: Private governance of multi-owned properties* (Routledge, 2017), 11.

[20] Cathy Sherry, "Land of the Free and Home of the Brave? The Implications of United States Homeowners Association Law for Australian Strata and Community Title", (2014) 23 *Australian Property Law Journal* 94

less likely to be a swimming pool or golf course, and more likely to be green infrastructure, including DER.

The third aspect of strata and community title that makes it attractive for DER is the existence of a separate body corporate. On the registration of a strata or community plan, a governing body corporate, made up of all lot owners is automatically created. Confusingly, the names of these bodies differ between states and even within a state – owners corporation, strata company, community association, precinct association, and neighbourhood association. However, they are all simply separate legal entities made up of owners (not tenants). When people colloquially talk about 'the strata', this is the body to which they are referring. Although the body corporate might be assisted by a strata and/or building manager, these people are simply agents. Ultimately, all power in a strata or community scheme rests with the body corporate.

Large community title schemes – master planned estates - can be 'tiered' and have multiple bodies corporate. For example, in NSW a large site might have an overarching community association, two subsidiary precinct associations, which in turn have further subsidiary neighbourhood associations and/or owners corporations. This allows the site to be physically subdivided into discrete sections and most importantly, to allocate costs appropriately. In the diagram below, each neighbourhood association may be a group of townhouses which share a pool, solar panels, battery, or other infrastructure. The communal infrastructure will be the individual neighbourhood association's common property, and as a result the owners have both exclusive use of it and exclusive responsibility to pay for it via levies. Other collectively used infrastructure, such as roads, pavements, parks and green infrastructure, might be part of the over-arching community association common property, accessible by all residents of the estate. Individual owners are members of their own body corporate (the strata owners corporation or neighbourhood association), and those bodies corporate are then members of the body corporate above them.



Sample governance structure in a tiered community scheme[21]

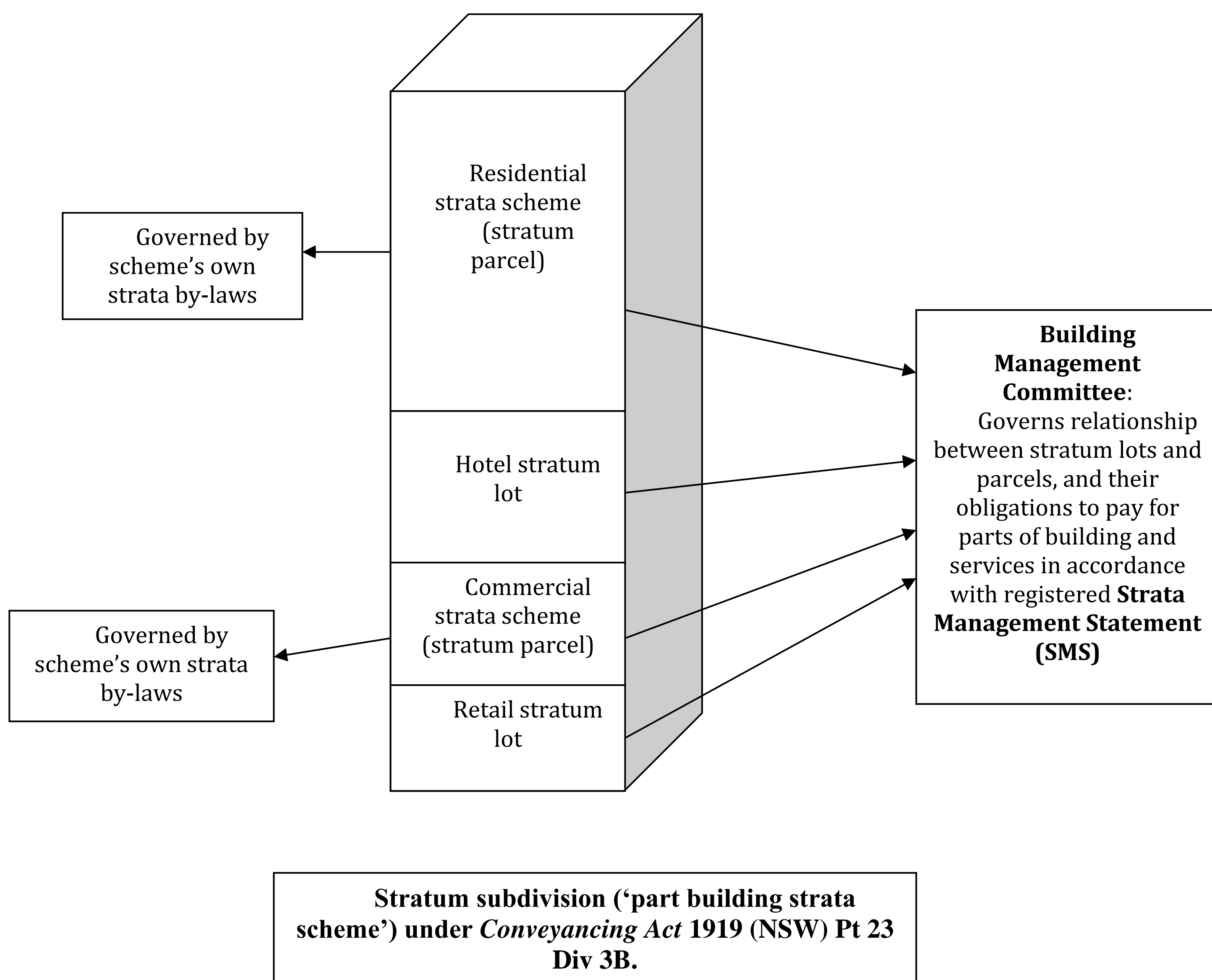
The final aspect of strata and community title legal structure that makes strata title attractive for DER is the existence of by-laws. All strata schemes are registered with by-laws or 'management statements' in community or neighbourhood schemes. These are entirely private regulation initially created by the developer, but subsequently alterable by the body corporate with special majority vote. While there are model by-laws in the legislation, developers are under no obligation to use them, and frequently do not, particularly in large strata schemes or master planned estates. They draft lengthy, bespoke by-laws/management statements that support the kind of community they wish to create and the facilities and services they want to provide.

For the sake of completeness, and because these developments are increasingly popular with developers, particularly for sustainable development, stratum subdivision needs to be explained. Stratum subdivisions are created under a brief section of the *Conveyancing Act 1919* (NSW), Part 23, Division 3B, and they facilitate mixed use development favoured by planners and government.[22] Individual buildings and land can be subdivided into ordinary Torrens lots, only some of which are then further strata

[21] Precinct schemes are in fact rare. The more tiers a community scheme has, the more complicated and expensive it is to run, and so lawyers try to avoid excessive layers of management.

[22] Stratum or volumetric subdivision is also possible in Queensland, under the *Land Title Act 1994* (Qld) (s 48D and Pt 4 Div 4) and in Victoria under the *Subdivision Act 1988* (Vic) (s 27).

subdivided.[23] The ordinary Torrens lots will typically have an investor owner who uses the lot for retail, commercial or even tourism purposes, while the residential component of the building will be a separate strata scheme with individual apartments and common property. The attraction of stratum subdivision is that it allows commercial owners to exist outside of a residential strata scheme and thus outside of the consumer protection provisions in the strata legislation. This diagram illustrates a simple stratum subdivision of a single building, although most stratum subdivisions are of buildings and land (often extensive):



Stratum subdivision ('part building strata scheme') under *Conveyancing Act* 1919 (NSW) Pt 23 Div 3B.

[23] Strata and community title are also Torrens title. The only alternative to Torrens title is Old System title, which is now non-existent in some states, and infinitesimal in all other states.

While the strata scheme will have common property, the overall stratum subdivision does not. However, being housed in a single building or development, all lots will need to share services and infrastructure such as lifts, chillers, pumps and fire equipment. These will be located on the property of a single stratum lot, and thus owned by the owner of that lot, but their shared use and costs will be regulated by a building or strata management statement (BMS or SMS). This is simply a document that is drafted by the initial developers' lawyer, and registered on the Torrens register. As a registered dealing it binds anyone who buys a lot in the development, including the strata owners corporation.[24] A BMS/SMS *must* contain certain matters such as insurance, damage and disputes, it *may* contain provisions on the appointment of a managing agent, trading activities, service contracts, and an architectural code, however it is not limited to this list.[25] It is a highly unregulated document,[26] and can contain provisions as surprising as the annual payment of $60,000 for the promotion of Italian cultural events, as the SMS did in the troubled and eventually failed Italian Forum development in Leichardt.[27] Like strata levying provisions, the costs schedule in a BMS/SMS overcomes the orthodox prohibition on positive obligations on freehold land, making it viable to install infrastructure and facilities in developments, including DER. In addition to maintenance provisions, BMSs must establish a 'building management committee' (BMC), made up of all stratum lot owners and any owners corporations, although owners can be excluded with their consent. Unlike a strata body corporate, a BMC is not a separate legal entity.

Stratum subdivision is the preferred legal form for developers doing complex, sustainable developments, the most well-known being Barangaroo and Central Park. Barangaroo, Australia's first carbon neutral development, includes a water recycling plant, 6000 square metres of solar panels and a centralized cooling system that takes

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[24] A basic principle of all Torrens legislation is that new registered proprietors are bound by whatever is already recorded on the register: *Real Property Act 1900* (NSW), s42.

[25] *Conveyancing Act 1919* (NSW), sch 8A cl 5(3).

[26] As a result of problems with inequitable BMS/SMS (see for example, *Owners Corporation Strata Plan 70672 v. The Trustees of the Roman Catholic Church for the Archdiocese of Sydney* [2011] NSWSC 973 and Cathy Sherry, 'Building management statements and strata management statements: unholy mixing of contract and property', [2013] 87(6) *Australian Law Journal* 393), the legislation was altered so that BMS/SMS must contain a 'fair' allocation of costs, and be reviewed every five years to ensure they remain fair: *Conveyancing Act 1919*(NSW), sch 8A, cl 2(1)(e1) and (e2).

[27] *Italian Forum Ltd v. Owners – Strata Plan 60919* [2012] NSWSC 89. See also, Cathy Sherry, *Strata Title Property Rights: Private governance of multi-owned properties* (Routledge, 2017), 142-148.

water from Sydney Harbour.[28] Central Park, the plant covered building near Sydney's Central Station, has a low carbon tri generation power plant and a black and grey water recycling plant, and was awarded a 5 green star rating. [29] All of that green infrastructure is private property that somebody has to own and maintain. Titles are allocated by the registered stratum subdivision plan and costs are allocated by the registered BMS/SMS.

Maximising developer profit: developer-made body corporate contracts

Two elements of strata, and similar property forms, are particularly attractive for developers. First, the existence of common property on which to site facilities and infrastructure, coupled with the legal obligation to pay for its upkeep through levies. As noted, that makes it viable for developers to provide infrastructure that will not simply fall into disrepair, and developers may generate greater profits from sales if facilities and infrastructure are attractive to investors and homeowners. However, that is a big 'if'. Residential sales prices are driven by factors that can have nothing to do with the residence itself, the most obvious being low interest rates which have fuelled a 30-year unbroken, property boom in Australia. Consumers have also become more wary of facilities like pools and gyms, which they now generally understand they will be responsible to maintain and repair. Finally, while people might be intellectually and morally committed to net zero, that does not necessarily translate to their hip pockets. Thus, the inclusion of facilities and infrastructure, green or otherwise, will not guarantee higher developer profit.

However, the second element of strata title will – the existence of a separate body, that a developer can cause to enter contracts that ultimate homeowners will have to pay. Those contracts can either be with a subsidiary of the developer, creating an on-going income stream, or with associate of the developer, who will provide the developer with a kickback in cash or kind.

Developers around the world have used this power in a range of ways, for their own benefit,[30] but the most notorious example in Australia is the management rights

[28] Barangaroo, 'Sustainability' https://www.barangaroo.com/past-present-future/a-21st-century-transformation/sustainability accessed on 27 October 2023.

[29] Frazers Property, 'Central Park, Sydney' https://www.frasersproperty.com.au/Our-Properties/Completed/NSW/Central-Park, accessed on 27 October 2023

[30] See Ann Dupuis and Jennifer Dixon Sarah Blandy (eds), *Multi- owned Housing: Law, Power and Practice* (Ashgate, 2010)

industry, concentrated in Queensland tourism.[31] In the course of constructing a development, the developer will negotiate with a management company to sell the 'management rights' with the result that developments look like tourist facilities, while in fact being individually owned strata title apartments.[32] 'Management rights' typically consist of a long-term contract to provide services to the body corporate such as cleaning, security, supervising common property, a right to run a letting pool for short-term tourists, ownership of a commercial or residential lot, and/or exclusive use of a foyer or reception desk. A management company will pay the developer for these rights, and the longer the contract that binds the body corporate and the more it allows the management company to charge, the more the management rights company will be prepared to pay the developer. The owners of apartments, who will ultimately have to pay for these services, are completely absent from the negotiations. Management and other contracts are theoretically disclosed to purchasers in contracts of sale, but because all initial sales in Australia occur 'off-the-plan', prior to the construction of the building or the finalization of any of the legal documents, what is 'disclosed' is typically the *possibility* of such a contract, with key provisions, such as costs, left blank. Further, disclosure is embedded in lever arch folder thick contracts that few purchasers or even their lawyers understand.

Management rights have caused considerable dispute when owners ultimately discover that they are paying for services that they do not want or need, or which do not represent value for money. Legislative reform has attempted to provide owners with some protection, for example by limiting what developers can do in the 'initial period' (the period in which the developer still controls a special majority vote of the body corporate) and by mandating that some developer-made contracts terminate at the first annual general meeting controlled by owners.[33] However, in practice, developers step around these provisions. Owners with no knowledge of the development itself or any experience managing complex development are given little choice but to ratify or novate the developer negotiated contract at the first annual general meeting, binding the

[31] Cathy Sherry, *Strata Title Property Rights: Private governance of multi-owned properties* (Routledge, 2017), 132-136.

[32] For example, Q1 on Queensland's Gold Coast, https://www.q1.com.au/ accessed 29 October 2023.

[33] For example, in NSW, building management contracts theoretically must terminate at the first annual general meeting if they were formed during the period of developer control: *Strata Schemes Management Act 2015*, s 68.

body corporate to a contract that has not been negotiated in their interest. In NSW, the Supreme Court has held that the sale of management rights is a breach of fiduciary duty by a developer, but this case law has had limited impact on development practice.[34] In Queensland, the developer's right to sell management rights is enshrined in legislation.[35]

Developer contracts and renewable energy: the embedded network experience

The ability for a developer to contractually bind a body corporate for its own financial gain has profound implications for a just transition to renewable energy. This has already been amply demonstrated by consumers' experience of embedded networks across Australia.

Embedded networks are private networks that provide electricity, hot or cold water or gas to a group of consumers. In theory, they allow for bulk purchase at a discount, via a single 'parent' connection point, with the savings being passed on to consumers. Groups of consumers are typically found in shopping centres, residential parks (caravan parks) and strata or community schemes; they may be property owners or tenants. Embedded networks have increased exponentially in NSW in the past decade, with two authorised retailers, seven exempt sellers and 900 households in electricity embedded networks in 2013 ballooning to 793 authorised retailers, 161 exempt sellers, and 95 400 households in electricity embedded networks and 64 325 households in gas embedder networks supplying gas and hot water in 2022.[36] Embedded networks have been facilitated by exemptions from the requirement to be an authorized network operator and authorized retailer under the National Electricity Law if the sale of energy is not the operator's core business or the cost of authorization outweighs the benefits to consumers.[37]

Embedded networks do not always use renewable energy or other green infrastructure, but they can and increasingly will. To facilitate the uptake of renewable energy, an

[34] *Community Assoc DP No 270180 v. Arrow Asset Management Pty Ltd* [2007] NSWSC 527, [229] (McDougall J)

[35] *Body Corporate and Community Management Act 1997* (Qld), ss112-113.

[36] New South Wales Legislative Assembly Committee on Law and Safety, *Embedded Networks in New South Wales*, Report 3/57, November 2022, ('*Embedded Networks in NSW* Report'), 12.

[37] Australian Energy Market Commission, *Final Report: Review of regulatory arrangements for embedded networks*, 28 November 2017, 22-24.

embedded network could purchase power from a solar or wind producer off-site or purchase or generate green energy on-site. For example, a strata scheme could have roof-top solar, or a community title scheme could have a large bank of solar arrays, producing energy for the common property and/or residents, as well as selling power back to the grid. Those arrays could be ordinary common property, managed and controlled by the body corporate, or common property over which an embedded network operator has contractual and by-law control.

It is the potential of embedded networks to facilitate renewable energy that drove the marked increase in their construction. Writing in 2017, the Australian Energy Market Commission (AEMC) identified the increased focus of local councils on sustainable and smart infrastructure as 'a significant catalyst for the establishment of larger-scale embedded network solutions at the precinct scale, and potentially, at a community scale in Australia'.[38] Councils created mandates and incentives for developers, including permission to build at higher density. Developers also perceived increase marketability of developments with smart, green facilities.[39] The increase in embedded networks to facilitate sustainability is set to continue. Stephen Angel, Network Development Manager, Jemena Gas Networks (NSW), told a NSW Parliamentary Inquiry in 2022 that 'embedded networks aren't just limited to energy and aren't just limited to gas. We are seeing there is potential there for larger precinct type models, particularly when we look at net zero carbon and innovation in that space'.[40] Victoria recently banned embedded networks in new residential buildings, with the exception of those that use 100% renewable energy, thereby guaranteeing the increased construction of renewable energy embedded networks.[41]

Why did Victoria create a general ban on embedded networks when they can produce savings for consumers and drive innovation? The answer is that despite initial government and developer enthusiasm, embedded networks rapidly obtained a very bad

[38] Australian Energy Market Commission, *2017 Retail Energy Competition Review*, 2017, 154

[39] Australian Energy Market Commission, *2017 Retail Energy Competition Review*, 2017, 151.

[40] Stephen Angel, Jemena, Transcript, *Report on Proceedings Before Legislative Assembly Committee on Law and Safey Embedded Networks in New South Wales*, Legislative Assembly, 12 August 2022, 35, ('Transcript 12 August 2022').

[41] *Electricity Industry Act 2000* (Vic) General Exemption Order 2022, Order in Council, Victoria Government Gazette, 4000 G 39 29 September 2022.

reputation, necessitating a Federal inquiry[42] and multiple state inquiries.[43] The 2017 AEMC Federal inquiry found that 'an appropriate balance between innovation, consumer protection, and access to retail market competition' was not being achieved and that the current regulatory framework was not fit for purpose.[44] The 2022 New South Wales Legislative Assembly Committee on Law and Safety Inquiry found that contrary to the theory of cheaper energy prices for consumers through bulk purchase, savings are not passed on to customers, who often pay higher bills inside a network.[45] The Public Interest Advocacy Centre (PIAC) suggested that,

> [e]mbedded networks are not designed to serve or support the interests of the people living in them. They are allowed in the hope that innovative operators will pass benefits on to residents, but they have become a mechanism for additional profit for developers and operators, leading to the rapid growth in their employment.[46]

The NSW Distribution Network Services Providers - Ausgrid, Endeavour Energy and Essential Energy - were scathing, stating that customers were being adversely affected in relation to reliability standards, connection standards, billing information, outage notifications, guaranteed service levels and appropriate protections for life support customers.[47] There were also serious concerns about the safety of high voltage embedded networks and the inability of the current regulatory framework to create a safe environment in the future with the increase in two-way flow of energy from DER.[48]

There have been particular problems with embedded networks for hot water, with the NSW inquiry hearing of a customer who had been billed $9700 for 14 months of hot water. This is a result of an inherent weakness in consumer protection legislation, also seen in strata legislation – 'clever' lawyers can step around static provisions. In this instance, while water and energy are both regulated, their combination – hot water – is

[42] Australian Energy Market Commission, *Final Report: Review of regulatory arrangements for embedded networks*, 28 November, 2017

[43] Victoria State Government, *Victorian Government response to the Embedded Networks Review*, July 2022; *Embedded Networks in NSW* Report.

[44] Australian Energy Market Commission, *Final Report: Review of regulatory arrangements for embedded networks*, 28 November, 2017, iv.

[45] *Embedded Networks in NSW* Report, 17.

[46] Douglas McCloskey, PIAC, Transcript 12 August 2022, 21.

[47] Francoise Merit, Endeavour Energy, Transcript 12 August 2022, 49-50.

[48] Francoise Merit, Endeavour Energy, Transcript 12 August 2022, 57.

not.[49] Customers in hot water embedded networks have been intentionally made to fall between the stools of the National Energy Customer Framework and the *Water Industry Competition Act 2006* (NSW) (WICA) leaving them with no consumer protection. The NSW Inquiry recommended that the NSW Government immediately ban the separate charging of hot water embedded networks and implement proper price protection measures.[50]

However, the problem of embedded networks cannot be solved with energy market regulation because this regulation does not go to the root of the problem – long-term contracts which the developer causes the body corporate to enter. The NSW Inquiry heard specific testimony on the problems of embedded networks in strata schemes, particularly for new schemes in which it is 'very rare' for there not to be one or more embedded network contracts.[51] Industry experts explained that energy and water infrastructure, including solar panels and EV charging, is installed in the building by an embedded network operator at no charge in return for the developer causing the owners corporation to enter into a long term contract with substantial fees.[52] While s132A of the *Strata Schemes Management Act 2015* (NSW) limits the length of electricity, gas and other utility contracts to 3 years, ss(4) was included to exempt embedded networks so as not to pre-empt recommendations from the AEMC Report. As a result, these contracts can last for decades, contain roll-over clauses, impossible penalty provisions for early termination (e.g., a requirement for the body corporate to pay for the infrastructure, plus 5-10 years' of the operator's profit), and create practical impossibility for consumers to change providers (denying them the alleged benefits of market competition).[53] Contracts can also prevent owners making green upgrades, or prevent them benefiting from existing green technology. In the case of one building

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[49] *Embedded Networks in NSW* Report, 19; Energy and Water Ombudsman NSW, 'Hot water embedded networks', March 2021, https://www.ewon.com.au/page/publications-and-submissions/reports/spotlight-on/hot-water-embedded-networks accessed 27 October 2023.

[50] *Embedded Networks in NSW* Report, 18.

[51] Stephen Brell, Strata Community Australia (SCA), Transcript 12 August 2022, 10.

[52] Glen Streatfeild, Transcript 12 August 2022, 41; Strata Community Australia (SCA) Submission 136 to New South Wales Legislative Assembly Committee on Law and Safety, *Embedded Networks in New South Wales,* 5.

[53] Strata Community Australia (SCA) Submission 136, 8; Glen Streatfeild, Transcript 12 August 2022, 47.

with solar panels installed by the developer, the owners could not ascertain who was benefiting from the 20-year solar contract, simply that it was not them.[54]

Contracts are presented to the owners corporation at the first annual general meeting – the point at which the developer no longer controls a special majority vote – and they are asked or actively 'coerced' into novating or ratifying the contract.[55] The Committee was given evidence of strata managers telling owners that they had until midnight to sign or their water or power would be turned off. Those managers have been installed by the developer and have a vested interest in doing the developer's bidding.[56] The developer's bidding will be to ensure the body corporate enters the contract or a clause in the developer-embedded network provider contract will be triggered, compelling the developer to pay for the hitherto free infrastructure.[57] These practices directly mirror those that have caused so much dispute with management contracts in the tourism industry, described above.

Several submissions stressed the importance of disclosure of embedded networks in sales contracts and leases, while Strata Community Australia (SCA), the peak body for strata managers, also recommended that developers be required to disclose any commission, rebate or ownership regime (i.e. kickback) given to the developer.[58] Disclosure is a time honoured but largely ineffective consumer protection mechanism in relation to land, particularly strata schemes. The theory is that if purchasers or lessees are made aware of burdens in relation to the land, they can make an informed decision about whether to acquire the land or lease. The theory has more holes than Swiss cheese.[59] First, disclosure assumes that consumers are able to read and understand complex contracts for strata and community title properties, which as noted, are typically a lever arch folder thick, being documents that regulate extremely legally and physically complex developments. While lawyers and licensed conveyancers can in theory advise on the legal structure, in practice it is unlikely that general practitioners or conveyancers understand the legal structures devised by specialist development lawyers.

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[54] Ms Eloise O'Connell, Submission 12.
[55] *Embedded Networks in NSW* Report, 35. Stephen Brell, Transcript 12 August 2022, 9.
[56] Glen Streatfeild, Transcript 12 August 2022, 46
[57] Stephen Brell, Transcript 12 August 2022, 12
[58] *Embedded Networks in NSW* Report, 36
[59] Cathy Sherry*, Strata Title Property Rights: Private governance of multi-owned properties* (Routledge, 2017), 62, 92-98, 136

It is even less likely that lawyers, conveyancers or purchasers understand the engineering complexity of large-scale developments with embedded networks, and the inevitable costs associated with running and maintaining them. Second, disclosure assumes that all relevant details will be disclosed. However, because new apartment sales always occur off-the-plan, prior to the construction of the building, the drawing of final architectural and engineering plans, and the finalization of infrastructure and the contracts in relation to them, key sections of disclosure documents, most importantly costs, are invariably blank. Third, disclosure assumes that it is possible to disclose the ultimate functioning and costs of complex engineering, energy and market systems which will change unpredictably over time. Fourth, and most importantly, disclosure assumes that a person who does not like what they are told can simply choose to live elsewhere. This has always been untrue in relation to land, although this may not have been as clear in the past as it is in Australia's current chronically tight housing market. Unlike other consumer items, land (housing) is an inherently finite and essential resource. There are not unlimited properties from which consumers can choose, and consumers do not have the option to choose nothing. Housing is a basic necessity for survival, as well as any kind of fully realized life.[60] Consumers, particularly tenants, have limited financial resources; jobs, family, and community ties limit consumers to specific areas; and consistency in market product limit genuine alternatives. Finally, if something is inherently unfair or exploitative, disclosing it does not miraculously make it fair; some things should simply be prohibited. As property theorist Joseph Singer argues,

> some relationships are out of bounds…some contract terms are off the table…[and] there are some things you should not ask of others; there are some demands that cannot justly be made in a free and democratic society.[61]

Unfortunately, it does not seem that the Committee or any submissions raised the fundamental flaw in disclosure as a means of consumer protection in this area, and the

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[60] Waldron, Jeremy, 'Homelessness and the Issue of Freedom' (1991) 39 *UCLA Law Review* 295.

[61] Joseph William Singer, 'Democratic estates: property law in a free and democratic society', [2009] 94(4) *Cornell Law Review* 1009, 1048.

Committee recommended that disclosure of embedded networks be included in leases and contracts of sale.[62]

At their core, third party operated embedded networks present the same risk of all privitisation, exposing privatisation's basic flaw – all private operators enter the market to make a profit, and that profit has to come from somewhere. While in theory it can come from technology and innovation, often it comes out of consumers' pockets. Contrary to standard assertions that the private sector is always more efficient and competent, that is frequently not the case, and at the extreme end, many private operators in emerging industries are 'cowboys', a concession that was readily made about the embedded network sector by government and industry witnesses at the NSW Parliamentary Inquiry. AEMC recognizes that privatizing infrastructure also creates structural risks when operators manage multiple sites. If one of these businesses fails - a real risk in an emerging industry with inexperienced operators - 'multiple sites in discrete locations around the country could be affected, impacting potentially thousands of consumers'.[63] Privatisaton of essential energy services presents one of the greatest challenges for a just energy transition.

<u>Can Embedded Networks Work?</u>

Embedded networks can be beneficial but only if they are negotiated for the benefit of the body corporate, the entity made up of owners who will pay the bills.[64] There are two ways to ensure this occurs – by imposing fiduciary duties on a developer negotiating a contract for the body corporate or by allowing the body corporate made up of owners to negotiate contracts for itself. In relation to the former, a fiduciary is prohibited from placing themselves in a position in which their own self-interest and their duty to the principal conflict or from making an undisclosed profit (secret commissions or kickbacks) from their position.[65] The New South Wales Supreme Court has already held that a developer owes a fiduciary duty a body corporate,[66] which is breached by the sale

[62] *Embedded Networks in NSW* Report, 34.
[63] Australian Energy Market Commission, *2017 Retail Energy Competition Review*, 2017, 179.
[64] Stephen Brell, Transcript 12 August 2022, 10.
[65] *Hospital Products Ltd v United States Surgical Corporation* (1984) 156 CLR 41.
[66] *Community Assoc DP No 270180 v. Arrow Asset Management Pty Ltd* [2007] NSWSC 527, [229] (McDougall J)

of management rights contracts. This principle applies equally to embedded network contracts sold by the developer.

In relation to a body corporate negotiating contracts itself, there is evidence that this results in beneficial arrangements. First, it is possible for existing schemes to be retrofitted with embedded networks and/or green infrastructure, facilitated in NSW by reduced voting thresholds for sustainability infrastructure.[67] The NSW Parliamentary Inquiry received no evidence that retrofitting by bodies corporate was a source of exploitation and dispute. Although a housing co-operative, rather than a strata scheme, Stucco, a not-for-profit housing co-operative jointly owned by Stucco, the Department of Family and Community Services and the University of Sydney, provides an example of a successful green embedded network retrofit.[68] The converted warehouse with eight apartments, and 40 residents, was retrofitted with solar panels and a battery, supported by an $80,000 innovation grant from the City of Sydney. The building now has a high level of energy self-sufficiency which consumers actually benefit from, being charged around 75 per cent of the pro-rated external tariff charged to Stucco at the parent connection point. Ironically, Stucco, which is clearly not in the primary business of retailing energy, had difficulty obtaining network operator and retailer exemptions because the exemption process is geared to for-profit embedded network operators.

Second, body corporate negotiation is possible at the inception of the development even if the developer has initially negotiated with a service provider. For example, the NSW Parliamentary Inquiry was given evidence of an owners corporation that was presented with a 15 year, $90,000 stormwater contract at their first annual general meeting. Fortunately, one owner had a procurement background and managed to persuade the other owners not to ratify the contract, despite the owners being told (presumably by the developer or an associate) that there was no other Australian provider and that their warranties would be voided if they did not sign. The owner with procurement experience swiftly found another provider at the cost of $1500 a year, a quarter of the cost of the developer-made contract.[69] On a financial level, this is a demonstration of the obvious fact that a contract negotiated by the person who will pay it is bound to be more

[67] *Strata Schemes Management Act 2015* (NSW), s5(1)(b)(ii) and s132B.

[68] Australian Energy Market Commission, *2017 Retail Energy Competition Review*, 2017, 155-156

[69] Karen Stiles, OCN, Transcript 12 August 2022, 13.

robust than a contract negotiated by a person who will not. However, on a social justice level, it is an example of 'the fundamental principle that owners should have the democratic right to decide how their collectively owned property will be used and…how people will live in their collective environment.'[70] It is consistent with the democratic values of modern property law, which after centuries of political and legal activism, wrestled control of land from feudal overlords and predecessors in title, vesting it in current owners and possessors.[71] Developer-made contracts create a form of predecessor control that is essential feudal.

Conclusion

Karen Stiles, Executive Director of the Owners Corporation Network (OCN), explained to the NSW Parliamentary Inquiry that 'since the turn of the century the New South Wales development industry has carefully characterised its interest as being in accord with the national economic interest to the point where consumer protection becomes roadkill in the corridors of parliaments.'[72] The power of the development industry to continue this practice will be infinitely enhanced by government and community commitment to meet net zero through the uptake of renewable energy and DER. To the extent that developers can align their financial self-interest with sustainability goals they will continue to ride roughshod over residential property owners and tenants, ensuring an inherently unjust and potentially ineffective energy transition.

Solutions cannot be found in energy market regulation alone. The privately owned DER that will be responsible for up to 45% of Australia's energy generation by 2050 is physical plant and equipment that has to be situated on *someone's* land and *someone* has to pay for its maintenance and use. Strata and community schemes, as well as stratum subdivisions, are prime targets for this infrastructure, with their collectively owned or shared land, and their statutory mechanisms for mandating payments. If we are going to ensure a just energy transition in the residential sector, we have to engage with the private property law that regulates the high density and master planned developments that Australians will increasingly call home. In doing so, we must ensure that

[70] Karen Stiles, OCN, Transcript 12 August 2022, 9.

[71] Joseph William Singer, 'Democratic estates: property law in a free and democratic society', [2009] 94(4) *Cornell Law Review* 1009; Cathy Sherry, *Strata Title Property Rights: Private governance of multi-owned properties* (Routledge, 2017), 51.

[72] Karen Stiles, OCN, Transcript 12 August, 9.

developers, as original owners of land, are not permitted to control the land, infrastructure, and energy services ultimately owned and paid for by the residents of that land.