MICHAEL TEYS
Strata Research & Training

ADDRESS

Low Carbon Net Zero Homes
APPG Leasehold and Commonhold Reform
House of Commons, Palace of Westminster
6 February 2023

Main points

- Ageing strata buildings in Australia are being renewed and retrofitted to reduce carbon emissions financed by owner contributions (levies), strata loans, and selling airspace development rights.

- Strata laws have been amended in Australia to assist owners renewing buildings, financing, and installing sustainability infrastructure, and to enforce statutory repair and maintenance obligations.

- The Law Commissions proposals to reinvigorate commonhold in England and Wales should make it easier for banks to fund retrofitting of sustainability infrastructure at affordable rates if they can be satisfied about the priority of securities and community association solvency.

Context

1. Commonhold in Australia is called strata. We have had strata for 60 years. We have over 340,000 strata schemes comprising more than 2.8 million units. The insured replacement value is more than one trillion dollars (Easthope, Thompson and Sisson 2020). Nearly half of Australia's occupied apartments are in New South Wales (47 %) (Australian Bureau of Statistics 2017). In the City of Sydney, 80% of its residents currently live in units – 15 times more than the national average (NABERS 2020).

2. Compact city planning has been prevailing orthodoxy of urban design policy in each of the major Australian cities since the mid 1990's advocating high-density mixed-use developments and urban renewal (Grodach and Limb 2020; Bunker et al 2017; Crommelin et al 2017). Strata title is the key mechanism to deliver medium density and high-density development (Troy et al 2015; Dredge and Coiacetto 2011). Randolph (2006) notes densification only took on a higher profile after strata legislation was introduced in the 1960s. Since 2016 strata developments have been the majority for new housing approvals in Australia (ABS 2016). In Sydney strata apartments are presently more than 65 % of all new housing approvals (ABS 2016).

3. 35 % of Sydney's commonhold housing stock is more than 35 years old (OCN 2022). The NSW State Government has identified the growing issue of strata dilapidation and the pressure to increase housing supply as significant, and interlinked policy concerns (Troy et al. 2015; Easthope and Randolph 2021).

4. Buildings are responsible for 50% of electricity use in Australia and represent 25% of national emissions. Up to 60% of energy consumption in large apartment buildings come from common areas and shared services. Around 25 % of shared costs are spent on utilities alone (NABERS 2020).

5. Australia is committed to be net zero carbon emissions by 2050, with an interim 2030 target of 42% less carbon than 2005. NSW has a faster target to cut carbon emissions by 50% by 2030. To help drive these targets renewable electricity generation and transmission is being built with the federal government committed to ensuring 82% of electricity will be from renewable sources by 2030.

First Point – Ageing strata schemes are being renewed and retrofitted by owner corporations financed by owner levies, strata loans, and selling airspace redevelopment rights.

6. Evidence of renewal and retrofitting for sustainability infrastructure is limited. A not for profit, Green Strata (Christine Byrne) pioneered support for owners corporations in this field from 2010. In recent years 'fee for service' consultancies and local authority funded programs have taken on this work and provide case studies of savings for ageing strata, for example WattBlock; NABERS; Green Star; Smart Green Apartments; Building Futures .

7. Apart from government rebates and assistance, there are three methods by which owner corporations are funding sustainability retrofits: levy contributions, strata loans, and the sale of airspace redevelopment rights. The simplest and most common method of financing retrofitted sustainability infrastructure is by levying owners in accordance with their proportional shares in the scheme.

   Strata loans in Australia have been offered in Australia for more than 15 years. They are used for building defect remediation, refurbishment, retrofitting sustainable infrastructure, and redevelopments. The market is however relatively small, circa A$500 million. Strata loans are not available from mainstream banks. Owners corporations in Australia are precluded from granting a mortgage or charge over common property. Consequently, rates are high and are currently just over 10 % pa. Historically, strata loan interest rates have run at about 5 % higher than variable home loan interest rates. Strata loans are available for terms of up to 10 years. strata loans are being used to remove and replace combustible cladding. In some cases, the NSW state government is paying the strata loan interest for eligible owners corporations.

   Owners corporations borrow money on this basis where not all members can afford the increase in levies to pay for the infrastructure. In Australia levies cannot be assessed differentially so there is no option for some owners to pay their share of a contribution up front with other owners taking a finance option via a facility organised by the owner corporation.

Loans are made on the security of the owner corporations' statutory obligation to raise contributions to meet its debts. There are three reasons why loans are made in Australia on this basis-

- the law precludes winding up of owner corporations in Australia until, among other things, all the debts of the owner corporation are paid,
- owner corporations in Australia are unlimited liability entities where owners jointly and severally guarantee the debts of the owner corporation and a judgement creditor has a statutory right to appoint an administrator to assess and collect contributions until the judgement debt is paid.
- Levies run with the freehold unit title so new owners become jointly and severally liable for levies that are outstanding on the date they become a member of the owner corporation.

8. There is an emerging market for the sale of airspace development rights by owner corporations where the proceeds of sale are being used by to fund retrofitting of sustainability infrastructure. See, for example Byairspace and ARAD.

Second Point – Legislation in Australia has been amended to assist owners renewing buildings, financing and installing sustainability infrastructure, and to enforce statutory repair and maintenance obligations.

9. To facilitate higher density and renewal of aging buildings the New South Wales parliament introduced law in 2015 to allow for the sale or redevelopment of buildings with a reduced threshold of 75 % owners. The legislation has been unsuccessful with only 1 scheme having used the procedure. However, between 2105 and 2019 there was an increase in unanimous terminations from 177

terminations in 2010-2014 to 308 in 2015 to 2019 which may be related to the passing of 2015 termination laws (Crommelin et al 2020).

10. To encourage retrofitting of sustainable infrastructure, legislation was passed in 2022 in New South Wales to make it easier to pass resolutions to improve common property by financing and installing sustainability infrastructure. Now more than 50 % of those entitled to vote must vote no to defeat such a resolution. It is too early to assess the impact of this reform.

11. A draft bill is on exposure for consultation that will allow regulators to issue enforcement notices to owner corporations that have failed in their statutory duties to repair and maintain common property. The statutory duty of an owner corporation in NSW extends to fixing building defects of the original developer. Forcing effective and timely remediation work will prolong building life.

Third Point - The Law Commissions proposals to reinvigorate commonhold in England and Wales will make it easier for banks to fund retrofitting of sustainability infrastructure at affordable rates.

12. The ability of an owners corporation to raise funds for special projects such as remediation of defects and retrofitting of sustainability infrastructure is always problematic because of the diverse interests and financial circumstances of the owners. The Law Commissions proposed reforms to allow commonhold associations to borrow money and give a mortgage over common property should make it easier to attract finance for retrofitting sustainable infrastructure on terms more favourable than strata loans.

13. It is worth noting that despite strong banking and institutional support for strata in Australia, traditional Australian banks will not lend directly to an owners corporation. This might be because owners corporations can't give mortgage

security. However, there may be other issues relating to competing interest of banks with mortgages over both common property and unit titles.

14. If banks are concerned lending to a commonhold association limited by guarantee, then steps should be taken to ensure that the mortgagors right to appoint an administrator is not defeated by a winding up application that triggers the owners limited guarantee protection.

Michael Teys is a researcher and presenter with City Futures Research Centre, University of New South Wales. He has a law degree and was a strata lawyer in Australia for 30 years. He holds an Australian Research Council scholarship for a Master of Philosophy (Built Environment).