

Green Leasing

Aligning Energy Efficiency Incentives for Tenants and Building Owners

Standard commercial leases often ignore energy efficiency, preventing building owners and tenants from sharing the benefits of comprehensive building-wide energy efficiency efforts. Behavioral actions and/or cost-saving upgrades are often not pursued because of fundamental disconnects in distributing the costs and benefits of this valuable work. Simple adjustments in lease contract provisions can overcome these barriers and align incentives, creating an “energy aligned” lease that results in energy and cost saving for all parties.

Background

In many commercial buildings, owners are responsible for the upfront costs of energy efficiency upgrades, but tenants are the sole beneficiaries of reduced energy bills. On the other hand, where building owners are responsible for all energy costs, tenants have no incentive to use less energy because they do not save money. These issues, known collectively as a “split incentive,” are caused by standard leasing provisions that fail to align the benefits of energy efficiency between owners and tenants. As a result, both parties often have little incentive to invest in energy efficiency.



Green leases encourage energy efficient practices by aligning costs and benefits between property managers and tenants.

Benefits

Overcome the Split-Incentive Barrier. There are many adjustments that can be made to standard leases that can motivate energy efficiency upgrades and energy-saving behavior. To overcome the split incentive, new lease language developed by the New York City Mayor’s Office with industry and environmental stakeholders creates an equitable sharing arrangement of energy efficiency costs and benefits between stakeholders. The lease includes an innovative expense pass-through clause that allows owners to recover the capital costs of efficiency upgrades from tenants more quickly than standard leases allow, but in a manner that protects tenants from performance issues and enables them to accrue energy cost savings immediately (see the *Existing Policies or Programs* section for more. Other lease specifications that can encourage energy efficiency include:

- Specifying the use of energy-efficient products in tenant space build-outs and operations.
- Sub-metering tenant spaces.
- Creating fee structures for the use of base building systems during non-standard business hours.
- Facilitating data sharing between owners and tenants to enable energy benchmarking.
- For tenants, establishing minimum energy performance standards for leased space.¹

Unlocking Community Economic Benefits. Energy aligned leases remove a major obstacle to private investment in building energy efficiency without the need for government dollars, helping spur energy-efficiency upgrades that create market-based demand for workers in the construction, building operations, engineering and design trades. Additionally, energy-aligned leases that reduce energy costs for occupants make those buildings more attractive to potential tenants, helping increase occupancy and asset values for owners.

Getting Started

Local jurisdictions should approach energy-aligned leasing in two ways: Educate private sector stakeholders and secure support for leasing provisions; and lead by example by integrating leasing provisions into their own leasing practices.

Step 1: Convene and Educate Private Sector Stakeholders.

Policymakers in New York City and San Francisco convened stakeholder groups comprised of real estate attorneys, leasing agents, building owners and other parties to discuss energy-aligned leasing principles and build consensus over the development of the provisions.² Jurisdictions should build upon the energy-aligned lease developed through this process in New York City and secure commitments from local real estate companies and associations to use energy-aligned lease provisions.

Step 2: Recognize Achievement.

Jurisdictions should hold media events and provide other recognition for involved parties when energy-aligned leases developed during the stakeholder process are signed. New York City Mayor Michael Bloomberg attended a signing ceremony for the first energy-aligned lease signed in New York.³

Step 3: Lead by Example.

Occupying energy-efficient buildings can save taxpayer money that local jurisdictions would otherwise spend on wasted energy. Local government agencies should integrate energy-aligned leasing provisions into their own leasing practices. New York City is using its energy-aligned lease in all new leases signed by the city. The state of Washington has established energy performance minimums for buildings where the state leases space. Leading by example will encourage private building owners to make their buildings more energy efficient to compete for government leases.

Existing Policies or Programs

New York City: PlaNYC - A Model Energy Aligned Lease Provision

http://www.nyc.gov/html/planyc2030/downloads/pdf/energy_aligned_lease_official_packet.pdf



- **Adopted:** Began as a pilot program in 2009.
- **Author:** New York City Mayor's Office of Long-Term Planning and Sustainability, Natural Resources Defense Council and industry stakeholders.
- **Lease Language:** A capital expense pass-through clause allows landlords to recoup 80% of projected energy savings from a retrofit project each year from tenants. The remaining 20% of cost savings accrue to tenants immediately and also act as a buffer in case the retrofit underperforms. Accordingly, the landlord's cost recovery period is extended by 25%.
- **Status:** Incorporated into a 200,000-square-foot lease at 7 World Trade Center in New York City in April, 2011. The lease provision is supported by the Real Estate Board of New York.

Washington State Energy Performance Leasing Requirement

<http://apps.leg.wa.gov/documents/billdocs/2009-10/Pdf/Bills/Session%20Law%202009/5854-S2.SL.pdf>

- **Passed:** April 2009 **Effective:** January 1, 2010
- **Affected Property Type:** State-leased commercial space greater than 10,000 SF where the state pays for energy expenses.



- **Key Requirement:**

- Washington state agencies must lease space only in buildings with an energy performance rating of 75 or greater on the EPA Energy Star benchmarking scale, or where the building owner conducts an energy audit and implements cost-effective energy efficiency upgrades within the first two years of the lease.

Energy Independence and Security Act of 2007

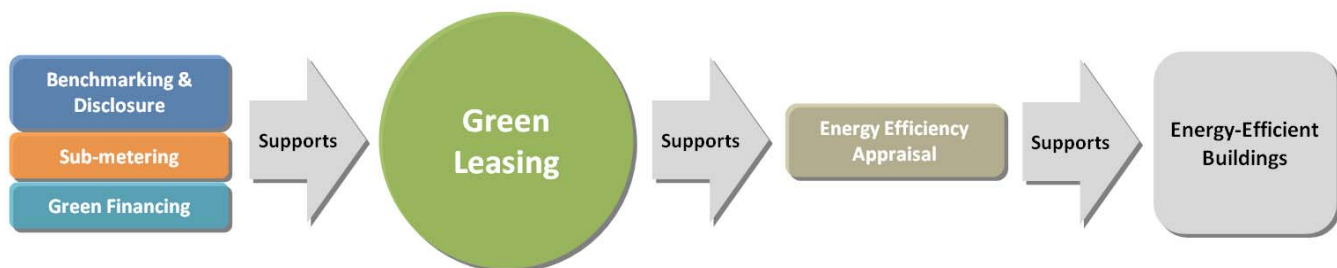
http://frwebgate.access.gpo.gov/cgi-bin/getdoc.cgi?dbname=110_cong_bills&docid=f:h6enr.txt.pdf



- **Passed:** Dec. 2007 **Effective:** Dec. 2010
- **Affected Property Type:** Federally leased commercial space greater than 10,000 SF.
- **Key Requirement:** Federal agencies must lease space only in buildings that have achieved the EPA Energy Star label, signifying a rating of 75 or greater on the Energy Star benchmarking scale, or where the building owner implements cost-effective energy efficiency upgrades to the space.

Complementary Policies

Complementary Policy Landscape for Green Leasing



Complementary policies can make green leasing much more effective.

- **Benchmarking and disclosure** policies use transparency to motivate energy efficiency coordination between landlords and tenants.
- **Submetering** individual tenant spaces is an important component of energy-aligned leases that increases tenant accountability for energy consumption.
- **Financing** options enable building owners to implement energy upgrades.

References

1. Greenbiz.com. "Why New Federal Leasing Rules are Good for Green Business." Jan. 5, 2011. <http://www.greenbiz.com/blog/2011/01/05/why-new-federal-leasing-rules-are-good-green-business>
2. "Mayor's Task Force on Existing Commercial Buildings: Final Report and Recommendations for the City and County of San Francisco." December 2009. http://www.imt.org/files/FileUpload/files/Benchmark/sf_existing_commercial_buildings_task_force_report.pdf
3. New York City Press Release. "Mayor Bloomberg Announces First Ever Lease for Commercial Office Space that Contains Groundbreaking Language that Incentivizes Energy Efficiency." April 5, 2011. http://www.nyc.gov/portal/site/nycgov/menuitem.c0935b9a57bb4ef3daf2f1c701c789a0/index.jsp?pageID=mayor_press_release&catID=1194&doc_name=http%3A%2F%2Fwww.nyc.gov%2Fhtml%2Fom%2Fhtml%2F2011a%2Fpr109-11.html&cc=unused1978&rc=1194&ndi=1

Additional Resources

- Building Owners and Managers Association (BOMA) Commercial Lease Guide.
<http://shop.boma.org/showItem.aspx?product=GL2011&session=628EFB2461EF469DBD2543FD3A5C94F8>
- Model Energy Aligned Lease Language (City of New York).
http://www.nyc.gov/html/planyc2030/downloads/pdf/energy_aligned_lease_official_packet.pdf
- National Standard Green Office Lease for Single-Building Projects (Real Property Association of Canada).
<http://www.realpac.ca/green-office-leases>
- “Energy Efficiency Lease Guidance to Address the Split-Incentive”.
<http://www.cycle-7.com/pdf/download.php?file=1297629475.pdf>
- Institute for Market Transformation.
<http://imt.org/green-leasing.html>
- U.S. General Services Administration Lease Policies.
<http://www.gsa.gov/portal/content/101755#nrg10-02>