Green Leases: Emerging Legal Issues for Commercial Landlords and Tenants
Best Practices For Negotiating and Crafting Environmentally Friendly Lease Terms

A Live 90-Minute Audio Conference with Interactive Q&A

Today's panel features:
Ronald B. Grais, Partner, Jenner & Block, Chicago
Michelle A. Neumann, Jordan Schrader Ramis, Lake Oswego, Ore.
Jacob Bart, Partner, Stroock & Stroock & Lavan, New York

Thursday, July 9, 2009
The conference begins at:
1 pm Eastern
12 pm Central
11 am Mountain
10 am Pacific

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Green Leases: Construction and Design Provisions

July 9, 2009

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A Green Building and a Green Lease Will Focus On:

- Reduced Energy Usage
- Reduced Water Usage
- Usage of Recycled Materials
- Healthy Internal Environments
- Integrated Waste Management Practices
Schedule “E”

Environmental Management Plan

Section 1 — ENVIRONMENTAL OBJECTIVES

1.1 Context

The provisions of this Environmental Management Plan have been designed to encourage and promote the implementation of certain environmental objectives on the part of each of the Landlord and the Tenant. Subject to Section 4.1 of the Schedule “E”, a breach by either the Landlord or the Tenant of any of the provisions of this Environmental Management Plan on the part of either the Landlord or the Tenant to be observed or performed, as the case may be, shall not constitute a default under this Lease, but the party committing such breach agrees, to the extent possible under the circumstances, to use commercially reasonable efforts to cooperate with the other party to remedy such breach.
General Objectives

• The Tenant acknowledges the Landlord’s intention to operate the Building so as to provide for:
  – a comfortable, productive and healthy indoor environment;
  – reduced energy use and reduced production, both direct and indirect, of Greenhouse Gases;
  – reduced use of potable water and the use of recycled water where appropriate;
  – the effective diversion of construction, demolition, and land-clearing waste from landfill and incineration disposal, and the recycling of tenant waste streams;
  – the use of cleaning products certified in accordance with EcoLogoM (Canada), Green Seal™ (United States) or equivalent standards;
  – the facilitation of alternate transportation options for individuals attending at the Building;
  – furniture and improvements within the Building and individual tenant premises; and
  – the achievement of such other more specific targets as may be set out in Section 1.3 below.
5.01 Environmental Performance Objective

The parties agree it is in their mutual best interest that the Building and Premises be operated and maintained in a manner that is environmentally responsible, fiscally prudent, and provides a safe and productive work environment.

5.01.1 The Tenant shall conduct its operations in the Building and within the Premises to minimize: (i) direct and indirect energy consumption and greenhouse gas emissions; (ii) water consumption; (iii) the amount of material entering the waste stream; (iv) negative impacts upon the indoor air quality of the Building and the Premises.

5.01.2 The Landlord shall operate and maintain the Building and the Premises to minimize: (i) direct and indirect energy consumption and greenhouse gas emissions; (ii) water consumption; (iii) the amount of material entering the waste stream; (iv) negative impacts upon the indoor air quality of the Building and the Premises.

5.01.3 The Landlord shall use its reasonable efforts to cause other tenants of the Building to conduct their operations in the Building and their premises in conformity with the Environmental Performance Objective.
Section 6.3 Sustainable Building Operations

(a) This building is or may become in the future [certified under the Green Building Initiative's Green Globes™ for Continual Improvement of Existing Buildings (Green Globes™-CIEB), the U.S. Green Building Council's Leadership in Energy and Environmental Design (LEED) rating system, or ______ standard or operated pursuant to Landlord's sustainable building practices]. [ADD THIS SENTENCE IF APPLICABLE: Landlord's sustainability practices address whole-building operations and maintenance issues including chemical use; indoor air quality; energy efficiency; water efficiency; recycling programs; exterior maintenance programs; and systems upgrades to meet green building energy, water, Indoor Air Quality, and lighting performance standards.] All construction and maintenance methods and procedures, material purchases, and disposal of waste must be in compliance with minimum standards and specifications, in addition to all applicable laws.

(b) Tenant shall use proven energy and carbon reduction measures, including energy efficient bulbs in task lighting; use of lighting controls; daylighting measures to avoid overlighting interior spaces; closing shades on the south side of the building to avoid overheating the space; turning off lights and equipment at the end of the work day; and purchasing ENERGY STAR® qualified equipment, including but not limited to lighting, office equipment, commercial and residential quality kitchen equipment, vending and ice machines; purchasing products certified by the U.S. EPA's Water Sense® program.
Sample Green Leasing Policy for “Responsible Company”

The Responsible Company has adopted a green leasing policy that guides its contracting strategies as they relate to leasing office space. The Responsible Company will adhere to the following practices when economically feasible.

**General Sustainability**
- Preferentially select a network of vendors that have expertise in sustainable practices
- Continually improve and upgrade water efficiency, energy utilization, and waste management within facilities
- Maintain a high level of internal expertise regarding sustainability
- Conduct regular financial analysis to assess the potential benefits of using or implementing more efficient equipment and practices in facilities

**Site Selection**
- Select sites that favor alternative means of transportation or shorter commuting distances for employees
- During the site selection process, the Responsible Company will measure and evaluate a site’s overall sustainability performance
- Preferentially select buildings with high ENERGYSTAR ratings

**Energy Efficiency**
- Use ENERGYSTAR and WATERSENSE products and equipment
- Take advantage of the utility company’s audit and incentive programs implementing cost-effective measures
- Utilize occupancy-based lighting control systems with appropriate zoning and daylight linking

**Water Utilization**
- Minimize water usage by landscaping with conservation-oriented plants (native, drought tolerant) and installing highly efficient water fixtures

**Waste Management**
- Promote recycling to the maximum extent possible
LEED CI Prerequisites

• Fundamental commissioning
• Reduced Energy Usage
• Elimination of CFCs in the mechanical system
• Storage and the collection of recyclable materials
• Minimum standards for indoor air quality and
• Prevention of smoking in non-dedicated smoking areas
Landlord Concerns

- Satisfaction of Construction Standard is “reasonable”
- Flexibility in maintaining rating level throughout lease term
- Tenant buildout will not reduce energy efficiency
- Tenant obligated to participate in building Environmental Management Plan
- Landlord able to recover costs of maintaining Green status

Tenant Concerns

- Can Landlord deliver the Construction Standard committed to
- Landlord must be obligated to maintain the Green Standard for the lease term
- Tenant operating obligations are realistic
- Limit Landlord’s annual reimbursement for Green expenditures
“Green” Fit-Out

- Lighting
- Floor finishes
- Walls & ceilings
- Casework
- Workstations
- General office furniture
- Kitchen fittings, appliances
- Paints, sealants, adhesives
- Bathrooms, toilets
- Supplementary A/C
- Submeters, “smart meters”
- Indoor plants
- Demo, construction waste mgmt.

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BOMA - Guide to Writing a Commercial Lease 2008
• All fixtures and accessories must be in compliance with EPAct of 1992. Lessor shall limit flow rates to 2 gpm for lavatory and multipurpose faucets and 2.5 gpm for kitchen faucets (at 80 psi). Lessor shall limit flow rates to 2.4 gpm for showerheads (at 80 psi). Lessor shall limit maximum flush volume to 1.6 gallons for toilets. Lessee shall establish usage reporting protocols with Lessor.

• Lessor shall install occupancy sensors to reduce energy consumption by switching off lighting fixtures in unoccupied areas, and coordinate all spaces for occupancy sensor control with the Lessee.

  – The Lessor will ensure that from the commencement date the Premises are separately metered for electricity (with the meters being digital electricity meters), gas and water services (both hot and cold). Lessor will ensure that the meters have an accuracy class suitable to customer billing and the meter register is readily accessible for billing. Lessor agrees that: (i) management of the meters will reside with Lessee on installation, if desired and (ii) Lessee is entitled to purchase its own electricity.
(a) Heating, ventilation and air conditioning ("HVAC") during Normal Business Hours, in season at such temperatures and in such amounts as to comply with ANSI/ASHRAE Standard 55-2004, Thermal Environmental Conditions for Human Occupancy, and ANSI/ASHRAE Standard 62.1-2004, Ventilation for Acceptable Indoor Air Quality. Air filtration shall be provided and maintained with filters having a minimum efficiency reporting value (MERV) as determined by ANSI/ASHRAE Standard 52.2-1999, Method of Testing General Ventilation Air Cleaning Devices for Removal Efficiency by Particle Size. Pre filters shall be have a MERV of 8 or higher, and final filters shall have a MERV of 14 or higher for all outside air intakes and inside air recirculation returns.
(b) The HVAC system which services the Premises shall be designed, installed and maintained in a manner which shall maximize its efficiency and shall, during Normal Business Hours, maintain the temperature of the Premises within the following range of temperatures, subject to unusual heat loads caused by Tenant's extraordinary use of the Premises or alteration of the Premises made contrary to the provisions of this Lease:

**Summer:**
- Outside: [93] Degree Fahrenheit Dry Bulb – [74] Degree Fahrenheit Wet Bulb
- Inside: [75] Degree Fahrenheit Dry Bulb – 50% Relative Humidity

**Winter:**
- Outside: [22] Degree Fahrenheit Dry Bulb
- Inside: [72] Degree Fahrenheit Dry Bulb – 50% Relative Humidity

Shell HVAC internal heat loads shall be based upon two (2) watts per rentable square foot (RSF) for lighting, two (2) watts per square foot for power and one (1) person per one hundred and fifty (150) RSF.

(c) Landlord shall make HVAC available to the Premises outside of Normal Business Hours in accordance with all applicable provisions of this Lease. Except during Normal Business Hours HVAC shall be furnished only upon request of Tenant, who shall bear the entire actual costs to Landlord to provide HVAC to the Premises. Tenant may request such HVAC service for one or more floors constituting the Premises. At Tenant's cost, Tenant may tap condenser water supply lines for supplemental HVAC services to Tenant's word processing and computer room units.
15. Purchasing

- Landlord has a comprehensive sustainable purchasing policy as part of its sustainability practices.

- In order to gauge Building performance, it is necessary for contractors to provide information about all material purchases for facility additions and alterations. Landlord will supply a standard formatting for reporting purposes that will include, but not be limited to, data on cost, recycled content, salvaged content, FSC-certified wood, rapidly renewable materials, and geographic origin.
1.3 Specific Objectives

1.3 Specific Objectives

- Notwithstanding the provisions of Section 1.2 in this Schedule “E” above, the Tenant acknowledges the Landlord's intention to achieve, and maintain, the following specific targets for the Building, by [NTD: target date if not today]
  a) electricity use averaging not greater than <*> kilowatt hours per square foot of Rentable Area of the Building per year (Kwh/sf/yr);
  b) natural gas consumption averaging not greater than <*> cubic metres per square foot of Rentable Area of the Building per year (M3/sf/yr)
  c) water consumption levels averaging not greater than <*> litres per square foot of Rentable Area of the Building per year (l/sf/yr); and
  d) a waste diversion rate not less than <*>% per year; and
  e) indoor carbon dioxide ("CO₂") levels compared to outdoor CO₂ levels of not greater than <*> Parts Per million (PPM) measured in accordance with the American Society of Heating, Refrigerating and Air-Conditioning Engineers ("ASHRAE") standard 62.1-2007 or equivalent standard as it may be amended or replaced from time to time.

1.2 Regulatory Standards

- Notwithstanding the provisions of Section 1.2 and 1.3 herein, in the event that any governmental authority imposes a resource reduction target on the Building for any utility or resource otherwise than as set out in Sections 1.2 and 1.3 above, then the within Environmental Objectives shall be deemed to have been amended so as to stipulate such resource reduction target and all changes required to be made by the Landlord to the Environmental Management Plan, or which are necessitated as a result of such mandatory resource reduction target, shall be deemed to be included and permitted, as the case may be, pursuant to the provisions of this Section and this Lease.
7.1 Heating, Ventilating, Air Conditioning, and Utility Consumption

(a)

(b) Any rebalancing of the climate control system necessitated by the installation of partitions, equipment or fixtures by the Tenant or by any use of the Premises not in accordance with the design standards of such system and/or the Environmental Management Plan shall be performed by the Landlord at the Tenant's expense. The Landlord shall not be responsible for inadequate performance of the Building Systems if: (i) attributable to: (A) any arrangement of partitioning in the Premises or changes therein; (B) the failure to shade windows which are exposed to the sun; (C) the production by the Tenant of smoke, odours or contaminated air which the Building Systems are not designed to accommodate; (D) any use of electrical power by the Tenant which exceeds the standard of normal use as determined by the Landlord or that as set out in the Environmental Management Plan; (E) any use of water by the Tenant which exceeds the normal use as determined by the Landlord or that as set out in the Environmental Management Plan; (F) any material deterioration in air quality as a result of any furniture, equipment, materials or improvements located in the Premises or the management practices of the Tenant or any other occupant or Person on the Premises which are not otherwise in accordance with the Environmental Management Plan; (ii) the occupancy level of the Premises exceeds one person to every 150 square feet of Rentable Area of the Premises on an open floor basis; or (iii) the Tenant does not keep the heating, ventilation or air-conditioning vents or air returns free and clear of all obstructions.

[Emphasis added]

2. Work Approval

- Contractor and all subcontractors must be approved to conduct their trades in the jurisdiction in which the Building is located by any and all governmental entities with such authority. Tenant or Contractor must provide Landlord with names, addresses and phone numbers for all subcontractors prior to commencement of work by the subcontractor. Construction drawings must be approved by Landlord prior to the start of construction. All projects shall be reviewed for potential impact to reduction targets and environmental programs. For any project over [$10,000], Contractor agrees to engage a third party Green Globe or LEED Accredited Professional or similarly qualified professional to oversee and validate that the project has met the standards for Landlord’s sustainability practices.

- An agent or representative of Contractor must be present on the site at all times when work is in process.
11. Construction Management Plan for Indoor Air Quality

Contractor agrees to develop and implement an Indoor Air Quality (IAQ) Management Plan for the construction and occupancy phases of the area being built out as follows:

- During construction, meet or exceed the recommended Design Approaches of the Sheet Metal and Air Conditioning National Contractors Association (SMACNA) IAQ Guideline for Occupied Buildings Under Construction, 1995, Chapter 3.
- Protect stored on-site or installed absorptive materials from moisture damage.
- If air handlers must be used during construction, filtration media with a Minimum Efficiency Reporting Value (MERV) of 8 must be used at each return air grill, as determined by ASHRAE 52.2-1999.
- Replace all filtration media immediately prior to occupancy.
- Remove contaminants that may be remaining at the end of the construction period.
  - Conduct a minimum two-week building flush-out with new filtration media with 100% outside air after construction ends and prior to occupancy of the affected space. After flush-out, replace the filtration media with new media, except for filters solely processing outside air.

Or

- After construction ends, conduct a baseline indoor air quality testing procedure for the affected space in the building that demonstrates that the concentration levels for the chemical air contaminants are below specified levels. For each sampling point where the maximum concentration limits are exceeded, conduct a partial building flush-out, for a minimum of two weeks, then retest the specific parameter(s) that were exceeded to indicate the requirements are achieved. Repeat procedure until all requirements have been met.
12. Optimize Use of IAQ Compliant Products

- Contractor agrees to develop an indoor air quality management program and to maintain it in conjunction with all construction projects in the Building as well as ongoing maintenance and repairs of the Building and Premises optimizing and documenting the use of air quality compliant materials inside the Building to reduce the emissions from materials used in the Building.

- Ongoing indoor air quality requires the use of low- or no-VOC paints, solvents, adhesives, furniture, and fabrics. Do not exceed the VOC and chemical component limits of Green Seal's Standard GS-11 requirements.

- Paints used on site shall be low-VOC and are to be brush-applied only; spray painting is not allowed on site. Paints must not exceed the VOC and chemical component limits of Green Seal’s Standard GS-11 requirements: interior non-flat $\leq 150$ g/L, Interior flat $\leq 50$ g/L.

- All painting must be completed outside of normal office hours (after 5:00 PM and before 7:00 AM) and on weekends.

- Carpet must meet the requirements of the CRI Green Label Plus Carpet Testing Program.

- Carpet cushion must meet the requirements of the CRI Green Label Testing Program.

- Composite panels and agrifiber products must not contain added urea-formaldehyde resins. Laminate adhesives used to fabricate on-site and shop applied assemblies containing these laminate adhesives must contain no urea-formaldehyde.

- Documentation of all covered materials purchased and the total cost of these purchases shall be provided. Documentation shall be provided in a format deemed acceptable to Landlord.
14. Energy Management

- Contractor agrees to install, calibrate and operate fundamental Building elements and systems as intended so they can deliver functional and efficient performance and leverage the Building’s energy management system. Contractor agrees to engage a commissioning authority independent from the design and construction responsibilities as the responsible party for all commissioning activities. All energy-related systems to be included in the commissioning process activities include as a minimum:
  - Heating, ventilating, air conditioning and refrigeration (HVAC&R) systems (mechanical and passive) and associated controls
  - Lighting controls, including daylighting
  - Domestic hot water systems
  - Renewable energy systems
- The building is currently Energy Star® rated; this rating is to be maintained at the highest level possible.
- All energy using equipment, appliances, lamps, ballasts and controls must be state-of-the-art energy efficient and Energy Star rated where available, conform to the Building’s then-current standards for energy management, and tie in to existing Building controls and monitoring systems.
- When available, Contractor shall install only ENERGY STAR® qualified equipment and appliances in the project, including but not limited to lighting, office equipment, commercial and residential quality kitchen equipment, vending and ice machines, and products certified by the U.S. EPA’s Water Sense® program. Documentation shall be provided in a format deemed reasonably acceptable to Landlord.
- Lamps and ballasts, including manufacturer, type, watts, and mercury content are specified and are to be replaced with “like” or better. Contractor shall reduce connected lighting power density below that allowed by ASHRAE/IESNA Standard 90.1-2004 by a minimum of 15%.
- Install daylight responsive controls in all regularly occupied spaces within 15 feet of windows and under skylights. Use occupant adjustable lighting controls.
- All energy-related improvements must be reviewed and approved by the Building’s chief engineer and/or energy manager.
16. Removal of Waste Materials

- Any and all existing building materials removed and not reused in the construction shall be disposed of by Contractor as waste or unwanted materials, unless otherwise directed by the Building Manager.

- Contractor agrees to provide documentation demonstrating that at least 70% by volume of any and all construction waste were recycled, salvaged or otherwise diverted from landfill and incineration.

- Contractor shall at all times keep areas outside the work area free from waste material, rubbish and debris and shall remove waste materials from the Building on a daily basis.
18. Housekeeping Practices

- Contractor agrees to use whole-building cleaning and maintenance practices, using:
  - Sustainable cleaning chemicals that meet the Green Seal GS-37 standard
  - Use of micro-fiber wipes, dust cloths and dust mops in place of paper wipes (and where paper products are used, use of products that contain at least 30% recycled content and which are recyclable)
  - Chemicals for which the GS-37 rating is not applicable, for example, floor finishes and strippers, shall be durable, slip resistant and free of zinc (metal-free) OR GS-40 and/or CCD-147
  - Carpet Care Products shall meet the requirements of GS-37 and/or CCD-148
  - Proper training of maintenance personnel in the hazards, use, maintenance and disposal of cleaning chemicals, dispensing equipment and packaging
  - Use of hand soaps that do not contain antimicrobial agents, except where required by health codes
  - Use of cleaning equipment that reduces impacts on IAQ

- Contractor shall provide a copy of a low environmental impact cleaning policy that meets these criteria. Contractor shall provide documentation that this policy has been followed, showing:
  - Specifications for chemicals used
  - Dates and activities associated with cleaning maintenance
  - Dates and outline of cleaning worker training.
• The Lessor’s design and construction team shall develop and utilize a construction and demolition waste management plan that identifies materials to be recycled and sources for their disposition. This plan must include new construction waste materials, packaging and associated clean-up activities and be approved by Lessee. Commonly recycled demolition materials include: asphalt, bricks, concrete and masonry, metals, wood, cardboard, carpet, gypsum drywall, and ceiling tiles. Lessor must divert X% of construction, demolition and land-clearing debris from landfill and incineration disposal.
Potential Legal Pitfalls In Green Leasing

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New Construction v. Existing Building

- New buildings - small part of the inventory.
- Existing buildings - may not seek any certification because of cost and timing, may instead adopt certain sustainability practices or seek EnergyStar rating.
- It is a challenge for owners of existing buildings to implement new practices without opportunity to modify existing leases.
Does going green contribute to the bottom line? New data emerging.

- Cascadia Green Building Council
  (http://www.cascadiagbc.org/news/GBValueStudy)

- RICS - “Doing Well by Doing Good”
  (http://www.rics.org/NR/rdonlyres/44F67595-7989-45C7-B489-7E2B84F9DA76/0/DoingWellbyDoingGood.pdf)
Potential Legal Pitfalls in Green Leasing

- Green leasing is a new and evolving area of the law - guidance and form documents are not fully established.
- New obligations unique to green leases can be difficult to identify.
Potential Legal Pitfalls in Green Leasing

- Once identified, obligations must be properly allocated and appropriate remedies established for breach.
- Term of lease and barriers to amendment present challenges for implementing green lease provisions.
Identifying new obligations of Landlord and Tenant

- Where do new obligations unique to green leasing come from?
  1. Evolving local, state, and federal requirements, incentives and initiatives relating to green building and sustainability.
  2. Certifications and rating systems.
  3. New operating procedures to improve energy efficiency or meet sustainability goals.
Evolving local, state and federal requirements, incentives and initiatives

- Developing rapidly. Happening now, with more on the way.
- Difficult to identify comprehensively.
Evolving local, state and federal requirements, incentives and initiatives

- “Various LEED initiatives including legislation, executive orders, resolutions, ordinances, policies, and initiatives are found in 44 states, including 198 localities (132 cities, 33 counties, and 33 towns), 33 state governments, 12 federal agencies or departments, 16 public school jurisdictions, and 39 institutions of higher education across the United States. (06/01/09)” – U.S. Green Building Council
  

- See link for state-by-state list.
Examples that have implications for commercial leases:

- City of Portland, Oregon – Proposed High Performance Green Building Policy
  [http://www.portlandonline.com/osd/index.cfm?c=45879&]

- For new commercial construction (buildings > 20,000 gsf, and major remodels > $250,000):
  - If you build to code – must pay a fee (based on gsf of building) to mitigate greenhouse gas emissions and other environmental impacts.
  - If you build to a green building standard (e.g. LEED) and improve energy performance beyond the minimum Oregon code – fee is waived.
  - If you achieve a high performance green building standard and significantly improve energy performance beyond the current minimum Oregon requirement – a reward is paid to the building owner.
Examples that have implications for commercial leases:

- For commercial buildings > 20,000 gsf - required *public disclosure* of environmental performance measures using Energy Star benchmark ratings.
  - Must participate in the Energy Star Portfolio Manager program (including reporting energy use, water consumption levels and indoor air quality).
  - Must disclose whether Building qualifies for Clean River Rewards storm water utility discount program and indicate extent of storm water managed on-site.
  - Buildings that do not achieve minimum rating of 30 for existing Buildings will be required to reach this minimum level or demonstrate a 15% reduction in energy use by the phase-in dates.
  - Buildings that do not comply will be subject to a fine of $.01 per gsf for every point below the Energy Star rating threshold.
Examples that have implications for commercial leases:

- Recent Metro (regional government) program requires local businesses to recycle all types of paper and certain containers such as plastic bottles, aluminum cans and glass. All local governments in the region were responsible for adopting the recycling requirements by February 2009.

- Fines are possible for non-compliance.

Examples that have implications for commercial leases:

- Washington, D.C. - among first cities to require privately owned buildings to meet LEED standards.
- District’s Clean and Affordable Energy Act of 2008 will require private building owners to annually benchmark energy performance of their Buildings - results be accessible to public through a website.

Examples that have implications for commercial leases:

- “A tax deduction of up to $1.80 per square foot is available to owners or designers of new or existing commercial buildings that save at least 50% of the heating and cooling energy of a building that meets ASHRAE Standard 90.1-2001. Partial deductions of up to $.60 per square foot can be taken for measures affecting any one of three building systems: the building envelope, lighting, or heating and cooling systems. These tax deductions are available for systems placed in service from January 1, 2006 through December 31, 2013.”

http://www.energystar.gov/index.cfm?c=products.pr_tax_credits#s8
Examples that have implications for commercial leases:

- Information on state, local, utility, and federal incentives that promote renewable energy and energy efficiency: [http://www.dsireusa.org/](http://www.dsireusa.org/).

(Database of State Incentives for Renewables & Efficiency is an ongoing project of the North Carolina Solar Center and the Interstate Renewable Energy Council (IREC) funded by the U.S. Department of Energy.)
Examples that have implications for commercial leases:

- Federal cap and trade legislation: Waxman-Markey bill - American Clean Energy and Security Act (H.R. 2454)
- In the United States, buildings account for:
  - 72% of electricity consumption
  - 39% of energy use
  - 38% of all carbon dioxide (CO₂) emissions
  - 40% of raw materials used
  - 30% of waste output (136 million tons annually)
  - 14% of potable water consumption

Identifying new obligations of Landlord and Tenant

Where do these obligations come from?

1. Evolving legal requirements, incentives, and initiatives relating to green building and sustainable business practices.
2. **Certifications and rating systems.**
3. New operating procedures.
Certifications and Rating Systems

- U.S. Green Building Council’s Leadership in Energy and Environmental Design (LEED)
- LEED 2009
- Green Building Initiative’s Green Globes
- EPA’s EnergyStar
Certifications and Rating Systems

- Obtaining
- Maintaining
- Re-certifying to a different standard
- Public reporting requirements
Certifications and Rating Systems

- Can the costs of registration and certification be passed through?
- Ongoing benchmarks for performance
  - How to verify?
  - What if not met?
- Tenant should ask – is this Building registered or planning to register?
- Is Tenant obligated to comply with requirements related to maintaining or obtaining a certification?
- Is Landlord obligated to seek or maintain a certification?
Certifications and Rating Systems

- Trends
  - The bar will rise. Standards are low now to encourage participation.
  - LEED-EB – more difficult to achieve if multiple tenants. Landlords seek to assist Tenant in obtaining some points under LEED-CI.
  - Greater focus on operations and performance, in addition to design and construction.
Identifying New Obligations of Landlord and Tenant

- Where do these obligations come from?
  1. Evolving legal requirements, incentives, and initiatives relating to green building and sustainable business practices.
  2. Certifications and rating systems.
  3. New operating procedures.
New Operating Procedures

- New operating procedures to improve energy efficiency, meet sustainability goals or meet changing legal requirements
  - green power, recycling, low VOC materials, green cleaning products, lighting usage, separate metering, gathering data and reporting performance, etc.
New Operating Procedures

- New operating procedures - relationship to operating expense provisions
  - Financial incentives in the lease for Landlord and Tenant to "go green" - pro-rata sharing of operating expenses – Tenant may lack financial incentive to go green.
  - Capital costs that the Landlord cannot pass through, even though Tenants receive the benefit in lower operating expenses.
  - Separate metering feasible?
  - Some recommend a gross lease.
  - Not all LEED-related costs contribute positively to the bottom line (green power, may be more expensive).
Alterations and Tenant Improvements

- Materials used, appliances installed (EnergyStar), reduction/recycling of construction waste.
- Are the costs related to a certification included in the improvement allowance?
Alterations and Tenant Improvements

- What happens if the LEED goal is not met? How to determine damages? *Southern Builders v. Shaw Development.* Address these issues clearly in construction contract for tenant improvements.

- Learning curve related to new systems, products, and methods. May be installation and performance issues.
Challenges in implementing green lease provisions

- Term of lease and barriers to amendment present challenges for implementing green lease provisions.
- Onerous requirements or lengthy new provisions may discourage transactions.
Implementing green lease provisions

- Clearly set forth the Building’s sustainability goals (including certifications, etc.) and each party’s respective obligations.
- Review language of lease.
- Add to standard lease form for building?
- Create a “green” addendum? Implement cooperatively with Tenant.
- Add new provisions at lease renewal?
- Implement through Rules and Regulations?
Other clauses implicated when “greening” a lease

- Use clause
- Assignment
- Parking
- Janitorial services
- Hours of operation; after-hours HVAC
Challenges in implementing remedy provisions

- How to monitor performance or compliance (failing to recycle, prohibited cleaning products, non-permitted materials or appliances installed)?
- How to determine if a default has occurred? “Aspirational” provision v. obligation.
- How to measure or prove damages?
  - How to prove energy costs higher?
  - How to prove HVAC not more efficient?
  - How to prove employees are less productive, less absenteeism?
  - How to prove air is not cleaner?
Remedies

- Pass-through of fines (e.g. mandatory recycling, failing to reach energy use benchmark).
- Reimbursement if operating expenses do not decrease. (Tenant could refuse to pay increase in operating expenses if Landlord cannot demonstrate a benefit.)
- Rent reduction.
Remedies

- Liquidated damages.
  - Reduction of asset value.
  - Adverse effect on brand.
  - Adverse effect on ability to attract other tenants, loss of rent premium.
- Remove non-complying improvements or appliances.
- Termination right – for Landlord or Tenant.
Potential Legal Pitfalls in Green Leasing - Conclusion

- No “one size fits all” solution.
- Track evolving local, state and federal requirements, incentives and initiatives.
- Keep certifications and rating systems in mind – for present and future.
- Consider effect on underlying economics of lease.
- Comprehensive review of all lease provisions.
- Determine best opportunity or method to incorporate green provisions.
Sharing of Costs and Obligations in a Green Lease

July 7, 2009

Jacob Bart
A. Operating Expenses
   i. First Dollar (Net)
   ii. Over Base Year (Gross)
   iii. General Exclusion of Capital Costs
       a) Operating and Maintenance Costs Included
       b) Costs of Ownership Excluded
          1. What Constitutes Cost of Ownership
          2. Improves Value; Benefit Inures to Landlord
   iv. Exception for Costs to Comply with New Laws
v. Exception for Costs to Achieve Savings
   a) Labor
   b) Energy

vi. Inclusion of Amortized Costs
   a) Straight line vs. Accelerated
   b) Useful Life vs. Length of Term
   c) Useful Life vs. Reasonable Investment Recovery Period
   d) Interest
      1. Fixed Rate
      2. Landlord’s Actual Borrowing Cost
   e) After Base Year (in Gross Leases)
vii. Caps
   a) Limited to Amount of Savings
   b) Absolute

viii. Exception for Costs to Achieve Green Benefits (other than Savings or New Laws)
   a) Retrofitting – “Split Incentive” Issue
   b) New Green Equipment – Allocation Required

ix. Express Inclusion of Monitoring and Studies Costs
x. Negating “Reasonable” Standard with Landlord Ability to Use Higher Cost, but Sustainable Energy Sources (e.g., “Green Power”)
   a) Open Standard with Landlord’s Reasonable Discretion
   b) Specific LEED Category Limitation
xi. Gross-up Issue
   a) What is a Gross-up of Operating Expenses?
      1. Generally 100% or 95%
      2. Inclusion of Base Year
   b) Needed to Make Landlord Whole
   c) All Operating Expense Items vs. Variable Items
### Allocation of “Green” Occupancy Costs between Landlord and Tenant

- **d)** If Variable, Landlord May Not Recover All Green Capital Items
- **e)** Compromise Possibilities to Incentivize Landlord (e.g., Inclusion with Caps)

#### B. Electricity Consumption in Premises

- **i.** Submetering vs. Rent Inclusion
- **ii.** Landlord Survey Right is Not Efficient Mechanism to Reduce Consumption in Rent Inclusion Lease

#### a) Landlord Profit Margin

1. Actual Use vs. Assumed Connected Load
2. Landlord Has No Incentive to Survey Unless Significant Increase in Electric Consumption
b) Tenant Has No Economic Incentive to Reduce Electric Consumption

iii. Converting from Rent Inclusion to Submetering
   a) Cost of Installation, Reading, Administration and Repairs
   b) Size and Configuration of Premises (Multi-Tenanted Floors)
GENERAL BUILDING OPERATION AND MAINTENANCE OBLIGATIONS

A. List of Lofty Goals (Not Necessarily All Achievable in Today’s World)

B. Landlord Obligations

i. Maintain Building to Specified Standard
   a) What Level of LEED (If Any) is Practical?
   b) Double Edged Sword

ii. Enforce Air Quality Standards by Methods Including Imposing Controls on Tenant Improvements in Premises (e.g., Carpet Glue)
   a) At Plan Approval Stage
   b) Monitoring Rights
GENERAL BUILDING OPERATION AND MAINTENANCE OBLIGATIONS

1. During Construction
2. During Post-Construction Occupancy
   c) Landlord Right/Obligation to Remediate
   iii. Create Procurement Requirements
   iv. Require (or Assume Cost of) Metering Wherever Appropriate
      a) Incentivizes Tenants
      b) Electricity
      c) Water
C. Tenant Obligations

i. Obligation to Install Energy Efficient Leasehold Improvements and Equipment

ii. Obligation to Use Recycled Materials
   a) What Level of Effort (Commercially Reasonable, etc)?
   b) Cost Considerations

iii. Tenant Willingness to Accept Restrictions in II.B(ii)

iv. Tenant Willingness to Accept Less Comfortable Base Building HVAC Specifications