

THE LEGALITIES: A Presentation and Discussion of Legal Concepts and Issues in Green Leasing

Presented by

Aaron M. Hyatt
(Brownstein Hyatt
Farber Schreck, LLP)

and

Mike Rooks
(Jones Lang LaSalle)

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“Greening” Existing Buildings

- Step #1: Do the Building’s existing leases provide Landlord sufficient flexibility to “green” the Building in the desired manner?
- Step #2: Assuming that the Building’s existing leases do not provide Landlord sufficient flexibility to “green” the Building in the desired manner, how can a Landlord implement “green” lease provisions into existing leases?

Analyzing Existing Leases – Generally

- The implementation of a “green” program will require “buy-in” from existing Tenants – whether voluntary or involuntary – as Landlords will likely seek to:
 - Pass-through certain of the costs associated with the “greening” process; and
 - Increase Tenants’ various obligations under the Leases in order to comply with the “green” program.
- The content of existing Leases will determine how aggressive a Landlord can be in extracting this “buy-in”.
- How “green” you want to go will likely dictate how much the Landlord can rely on existing lease provisions to implement a “greening” program.

Analyzing Existing Leases – Required or Desired Lease Provisions

- Operating Expenses. Do the leases' operating expense provisions permit Landlord to pass through capital improvements? If so, what portion of the capital improvements associated with the “green” program can be passed through?
 - Cost-Saving Improvements (e.g., improvements that are intended to reduce Operating Expenses).
 - Required Capital Improvements (e.g., improvements required to comply with changes in laws).

Analyzing Existing Leases – Required or Desired Lease Provisions

- Design and Construction Standards. Do the leases contain sufficient design and construction standards to obligate tenants to design and construct tenant improvements in accordance with the “green” program?
- Rules and Regulations. Are the leases’ rules and regulations provisions broad enough for a Landlord to introduce a “green” program and compel the tenants’ compliance?

**My leases do not provide me the
flexibility I need to implement a
“green” program in a desired fashion –
now what?**

Implementing “Green” Lease Provisions Into Existing Leases

- Obtaining the Tenant’s Buy-In:
 - Extol the Virtues of Going “Green”.
 - Reduced energy costs and other cost-savings;
 - Marketing and brand-enhancement (e.g., tenants can “sell” their commitment to “green” philosophies); and
 - Increase the value of a tenant’s lease (e.g., easier to sublease and/or assign a “green” lease).
 - Buy the “Buy-In”. If a tenant’s “buy-in” cannot be obtained through persuasion, a Landlord may need to buy a tenant’s cooperation through economic and other concessions.

Implementing “Green” Lease Provisions Into Existing Leases

- The “Green Lease” Addendum. Landlords will need to create form lease amendments that contain all the items necessary in order to implement and operate the green program.
- Risks to Landlords. Sophisticated tenants will look to extract something from a Landlord in exchange for the tenant’s cooperation.

Specific Lease Provisions: The Environmental Management Plan

- The Environmental Management Plan. A comprehensive plan that addresses various elements of a Building's "green" program. Like standard rules and regulations, the Environmental Management Plan needs to be flexible and can be amended from time-to-time to adapt to changing requirements and standards.

Specific Lease Provisions: The Environmental Management Plan

- The Environmental Management Plan should address, among other items:
 - Compliance with a general environmental standard;
 - Recycling obligations;
 - Air-quality and –temperature management;
 - Use of energy-efficient improvements (e.g., motion-sensor light fixtures, low-volume water fixtures, ENERGY STAR®-qualified equipment, etc.); and
 - Sub-metering or “smart”-metering of utilities.

Specific Lease Provisions: The Environmental Management Plan

- The Environmental Management Plan is in many ways the controlling element of a Building's "green" program.
- As a result, Landlords will likely want to retain an environmental consultant (e.g., LEED-certified professional, Green Globe professional, etc.) to assist with the creation and maintenance of a Environmental Management Plan.

Specific Lease Provisions: Operating Expenses

- Operating Expenses. What costs associated with a “green” program may or should be passed through to tenants?
 - Capital Improvements:
 - Cost-Saving Improvements (e.g., improvements that are intended to reduce Operating Expenses);
 - Required Capital Improvements (e.g., improvements required to comply with changes in laws); and
 - All capital improvement costs associated with implementing, monitoring, updating and complying with the Environmental Management Plan.

Specific Lease Provisions: Operating Expenses

- The Environmental Management Plan: Landlords will want to be able to pass through all costs – not just capital improvement costs – of implementing, monitoring and updating the Environmental Management Plan (e.g., fees and costs paid to professionals engaged to create and monitor the EMP).
- Caps on “Controllable” Operating Expenses: Landlords will want to classify all “green” costs as “uncontrollable” and therefore not subject to any year-over-year caps on “controllable” operating expenses.

Specific Lease Provisions: Utility Consumption

- Consumption “Targets” or Requirements: Soft “targets” or hard requirements that set forth specific utility consumption levels. For instance:
 - Electricity use averaging not greater than [xx] kilowatt hours per square foot per year (Kwh/sf/yr);
 - Natural gas consumption averaging not greater than [xx] cubic meters per square foot per year (M3/sf/yr);
 - Water consumption levels averaging not greater than [xx] cubic meters per square foot per year (l/sf/yr);
 - A waste diversion rate not less than [xx] % per year; and
 - Indoor carbon dioxide (CO₂) levels compared to outdoor CO₂ levels of not greater than [xx] parts per million (PPM) measured in accordance with the American Society of Heating, Refrigerating and Air-Conditioning Engineers (ASHRAE) standards 62.1-2007 or equivalent standards.

Specific Lease Provisions: Utility Consumption

- Sub-metering and “smart” metering. Landlords will want the ability to require the use of sub-meters or other “smart”-metering techniques to monitor and meter utility consumption – even if the Tenant’s use is not excessive.
- Landlord’s right to survey and inspect utility consumption. Landlords will want the ability to survey and inspect a Tenant’s utility consumption – by entering the Premises or otherwise.

Specific Lease Provisions: Alterations & Repairs

- Alterations & Repairs:
 - Generally. All alterations and repairs performed by or on behalf of Tenant will need to be in compliance with the Environmental Management Plan.

Specific Lease Provisions: Alterations & Repairs

- Alterations & Repairs:
 - Procurement & Contractor Requirements. Obligation to:
 - Use equipment and materials that comply with the Environmental Management Plan (e.g., motion-sensor light fixtures, low-volume water fixtures, ENERGY STAR®-qualified equipment, etc.); and
 - Engage, or to cause Tenant's contractor to engage, a third-party Green Globe or LEED-accredited professional to oversee and validate that the alterations conform to and comply with the Environmental Management Plan.

A Tenant's Perspective:

- What retrofitting and “green” costs should a Tenant pay?
 - Costs that actually reduce Operating Expenses or otherwise add value to Tenant.
 - Costs incurred due to changes in laws.
- What obligations should be imposed on Landlord as part of a “green” program?
 - Landlord should be required to comply with the Environmental Management Plan – especially as it relates to Common Areas.
- What concessions can I extract in return for agreeing to go “green”?

Conclusion

- As many existing leases will not provide sufficient flexibility to mandate compliance with a “green” retrofit, Landlords will be required to either (i) obtain tenant “buy-in” or (ii) entirely self-fund the cost of implementing the “green” program.

Conclusion

- New Buildings. As obtaining an existing tenant's "buy-in" will often be a Landlord's biggest challenge, owners of new construction are at an advantage as they can craft their lease documents in advance to address these issues.
- New Leasing. Correspondingly, an owner that intends to retrofit an existing building can revise its existing lease documents on a go-forward basis to address these issues in connection with new leasing activity.

Contact Information:

Aaron M. Hyatt
Brownstein Hyatt Farber Schreck, LLP
410 17th Street, Suite 2200
Denver, CO 80202-4432
ahyatt@bhfs.com
303.223.1107

Mike Rooks
Jones Lang LaSalle
1125 17th Street, Suite 1420
Denver, CO 80202
mike.rooks@am.jll.com
303.572.1800