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REPORT

Green Buildings

Industry Experts Hash Out Trends, Benefits, And Future of Green Building at BNA Webinar

Capital investment in green real estate will provide better returns than the overall commercial real estate market, according to a panel of experts who spoke Dec. 2 at the BNA-sponsored ''Green Building Practices: Legal, Financial, Technical Drivers in the Marketplace'' webinar. The panel described how building owners and managers can reap excellent returns on both ''green'' building retrofits, and properties built with green features.

In addition, participants described a new type of ''green'' mortgage-backed security and underwriting process, and one expert noted that it will be increasingly difficult for buildings to maintain a ''Class A'' rating without incorporating green features.

Green Retrofits a Smart Investment. One fast-growing sector of the green building market is the retrofit of older buildings with green features, said Leanne Tobias, founder and managing principal of Malachite LLC, a green building consulting company. ''Retrofits typically provide very strong returns on investment and payback; it's good business to undertake building retrofits,'' said Tobias. Retrofits can encompass anything from a complete gutting of a structure to ''a limited retrofit that can use very rapid and cost-effective solutions to reduce energy usage in a building.'' Tobias said benefits from green retrofits included ''increased building values, simultaneous repositioning, enhanced branding, and market results.''

The amount of green real estate is expected to climb rapidly over the next five years, said Tobias, with the approximately 6 billion square feet of currently green commercial and residential real estate booming to an expected 53 billion sq. ft. in 2015. This growth mirrors the increase in overall energy efficiency spending in the United States. That level stands at $25 billion per year now, but is expected to grow at a 9.3 percent rate through 2014, to $45 billion per year, said Tobias. Right now, building retrofits emphasizing energy efficiency make up about 70 percent of all building retrofits, and Tobias said that will continue to rise to about 90 percent by 2014.

Priorities Different for Owners, Tenants. The main motivation for building managers and owners undertaking green retrofits is ''energy cost savings,'' Tobias said. ''About 90 percent of building managers say that their key driver for undertaking a green retrofit is to reduce energy costs. [For] building owners [it's] about 80 percent.'' But the main factor for tenants and building occupants engaging in green retrofits is ''health and comfort; about 90 percent of building tenants say that their driver is a healthy indoor environment. About 80 percent say it's daylight and views,'' said Tobias, who added that 60 percent of tenants also cited energy efficiency as a reason for a green retrofit.

Tobias said tenant preferences in green retrofits are important for landlords to be aware of, especially because green improvements affecting health and comfort of building occupants tend to be easier and cheaper to implement. Improvements such as ''healthy finishes in a building, paints, carpets, wall coverings that do not let off gas, that do not introduce toxic residues into the environment,'' have become less expensive, in some cases consistent with conventional products, according to Tobias.

Capital Improvements Can Pay Off. While usually more expensive than comfort and health improvements, capital improvements to buildings reducing energy usage are economically viable, said Tobias. Energy efficiency retrofits generate a return on investment (ROI) in the range of 20 percent to 25 percent, said Tobias, with full payback occurring in four to five years. Green capital improvements as a whole exhibit slower returns, about 5 percent to 10 percent per annum, according to Tobias, but still achieve payback in six to 10 years. Some typi-

cal examples of capital improvements Tobias gave were:

- installing lighting sensors;
- implementing energy load reduction programs;
- mechanical tune-ups of buildings and building systems;
- improvements to ventilation systems;
- upgrades to heating and cooling systems; and
- building envelope improvements.

For those investigating or attempting a green retrofit, Tobias encouraged the use of well-established standards, like Leadership in Energy and Environmental Design (LEED) and Energy Star as guides. In addition, Tobias said that designing green improvements at the beginning of the overall retrofit planning was important. ''You'll get a better outcome,'' he said. Finally, Tobias advised owners to make sure their leasing and sales staff were aware of and trained in how to market the green features of the retrofitted property to maximize sale and lease value.

Green CMBS, Underwriting. A new method of financing green buildings and green improvements is through the use of green commercial mortgage-backed securities (CMBS), according to Mike Italiano, president and chief executive officer for Market Transformation to Sustainability. The economic potential of these securities is large, Italiano said. ''Green building securities can provide a $1 trillion stimulus,'' he said, while blunting the economic risks global climate change poses.

According to Italiano, rising prices for conventional forms of energy like coal, oil, and natural gas will have a definite impact on building prices, with more efficient buildings increasing in value, and less efficient ones decreasing as they become more expensive to operate. Italiano said that Wells Fargo identified obsolescence risk as a major concern for conventional buildings.

Italiano said his firm was developing underwriting standards for green building securities, under the review of the Federal Reserve Board and the U.S. Treasury Department. The success of green building securities will depend on sound underwriting standards, said Italiano, and would include a weighted score for each building, with certain green attributes or standards that increase value and decrease risk adding to a building's score. Some of these elements include:

- efficiency;
- proximity to transit;
- integrative design;
- commissioning of the building;
- improved indoor air quality;
- climate neutral operations; and
- compliance with green building standards such as LEED and Energy Star.

The elements that impact the green building underwriting score the most were those that increased revenue or decreased expenses, said Italiano, such as high energy and water efficiency, and on-site energy generation.

Government Policy. Michael J. Zimmer, of counsel at Thompson Hine LLP, outlined several government policies that will influence the direction of green buildings and retrofits going forward. Presidential executive order 13154 will have ''a major impact on development and momentum for net zero energy buildings, additional energy building research, as well as increased focus on green house gas reduction in both civilian and defense sector products and services and leases,'' said Zimmer.

Following the surge of Republican victories at state and national level elections, Zimmer said there would be ''more focus on tax incentives, perhaps additional energy programs, compliance codes, and the use of the government procurement processes'' to spur green development. This would be a shift away from ''grants, local/state funding, and transition grant funding,'' said Zimmer.

State building codes will also be seeing a shift, according to Zimmer, towards more reliance on international standards for guidance in green areas. Even cities are starting to implement green building code requirements, said Zimmer, using New York City as a recent example. ''They aren't waiting, necessarily, for the states to adopt the code improvements . . . New York has provided five building blocks for the future in existing buildings,'' said Zimmer. These five ''building blocks'' include requiring benchmarking, periodic audits, retro-commissioning, phased lighting improvements, and tenant submetering.

New markets for green buildings are also opening up, said Zimmer, with universities, government, and military instillations, IT [information technology] data centers, and ''the whole healthcare sector'' investigating the possibilities of greening their real estate. Zimmer said, ''Energy Star labeled leasing is now going to become the norm this month in federal government buildings, and a number of markets built with [non-governmental organizations].''

BY ERIC TOPOR

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