

Green leases progressing from an aspirational goal to the industry standard

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How to design a green lease

Over the next several years, real estate professionals will see green leases progress from an aspirational goal to the industry standard.

Currently there is no generally accepted agreement on the contours of a green lease, as real estate professionals debate the best approach. Should we "green" an existing form lease by inserting specific new clauses or start from scratch and create a new lease holistically?

Some guideposts are beginning to emerge in both the U.S. and elsewhere, including language from the Building Owners and Managers Association, the Real Property Association of Canada, and various riders and inserts promulgated by government authorities for use in their space leases. This article highlights some of the key provisions of a green lease.

"Net" vs. "Gross" Lease

There is debate over whether the goals of a green lease are served best by using a traditional "net" lease structure or a traditional "gross" lease structure so as to properly motivate both parties to achieve maximum energy efficiency.

I propose a two-step solution. First, use a "modified gross" form of lease, which includes a "base" amount of operating expenses in the stated rent, but passes through to tenants any annual escalations over this base amount. This way tenants will have some incentive to conserve energy (and reduce "above-base" payments) and the landlord will have some incentive to run a more energy-efficient building and to incur costs of implementing cost-savings conservation measures. Second, the lease should permit the landlord to pass the cost of these capital improvements through to tenants on an amortized basis as part of operating expenses.

Defining Relevant Standards/Requirements

Both the landlord and the tenant should be required to comply with the requirements of the green certification/rating applicable to the building in the course of their construction, alterations, maintenance, and business operations. In addition, the lease should define specific "Environmental Management Practices" in an exhibit. These could include any specific requirements required to maintain applicable green certification/ratings; descriptions of the building recycling and waste separation programs; and materials and procedures to be used in cleaning and maintenance operations. The important thing is that these requirements apply equally to the landlord and the tenant.

Tenant Buildout/Alterations

Where the building and/or the tenant's premises has obtained a green certification or rating, the landlord should require all tenant buildout and alterations to be performed in compliance with the requirements. In appropriate cases, the landlord should consider requiring the tenant to engage a

LEED Accredited Professional or other qualified professional to participate in the tenant's design and construction process to ensure conformance with these requirements.

The landlord should also require "green" procedures and technologies - such as compliance with the landlord's recycling and waste-separation programs during construction, use of occupancy sensors (for lighting), use of low- or no-VOC paints, solvents and adhesives, and use of recycled materials - for all construction projects. The lease should also require tenants to address projects opportunities to increase energy savings and/or sustainable design attributes.

Tenant Operations

The landlord should require the tenant to take "green" steps, such as using energy efficient light bulbs and ENERGY STAR rated equipment; closing shades to avoid overheating; complying with building-wide recycling and waste-separation programs; and turning off lights at the end of the day. The landlord should consider reserving the right to enter into the tenant's premises to monitor compliance with its "Environmental Management Practices." Where possible, the landlord should include energy management systems and sub-metering or other technologies to monitor electricity consumption by each tenant so that these charges can be billed back to individual tenants.

Breach of "Green" Provisions

The consequences of a breach by a party of the "green" obligations need to be addressed. Is every such breach a default under the lease entitling the other party to bring the full panoply of default remedies to bear, or should some of these be expressly provided to be of less consequence (e.g., simply require the breaching party to make "best efforts" or "commercially reasonable efforts" attempt to cure the breach and to prevent a recurrence)?

As you can see, the evolution of the green lease will be a dynamic process. Both landlords and tenants will have to adapt to new rights and obligations. Hopefully the resulting lease documents will provide clarity and certainty for both parties.

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