Getting your property strategy fit for a sustainable future

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Points to be covered:

1 Current market

2 Relevant legislation

3 Property strategy

4 Sustainable finance

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Current market

Occupation on the increase

- Office headcount expected to increase of pre-pandemic levels with 140,000 new office based jobs created according to CBRE market outlook for 2022
- RICS survey also confirms increase in occupier demand across all sectors

Type of accommodation required

- Rush to prime
- Excess of older accommodation
- Return of the rent free period

Employee expectations

- Office to support hybrid working
- Property to reflect and enhance your organisation’s ESG agenda
- Destination office

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What does the future hold

Hybrid Working

JLL claim this is now the expectation of 60% of office workers with 55% already working this way.

Work life balance and wellbeing are driving factors

Climate crisis and net-zero

Buildings responsible for c.17% of national emissions, the majority of which come from heating.

Government and organizational strategies to reach net zero

Cost of living crisis

Effect yet to be seen but increase in the cost of utilities and living costs could affect the office market and occupational rates

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EPC Legislation

Energy Performance of Buildings (England and Wales) Regulations 2012:

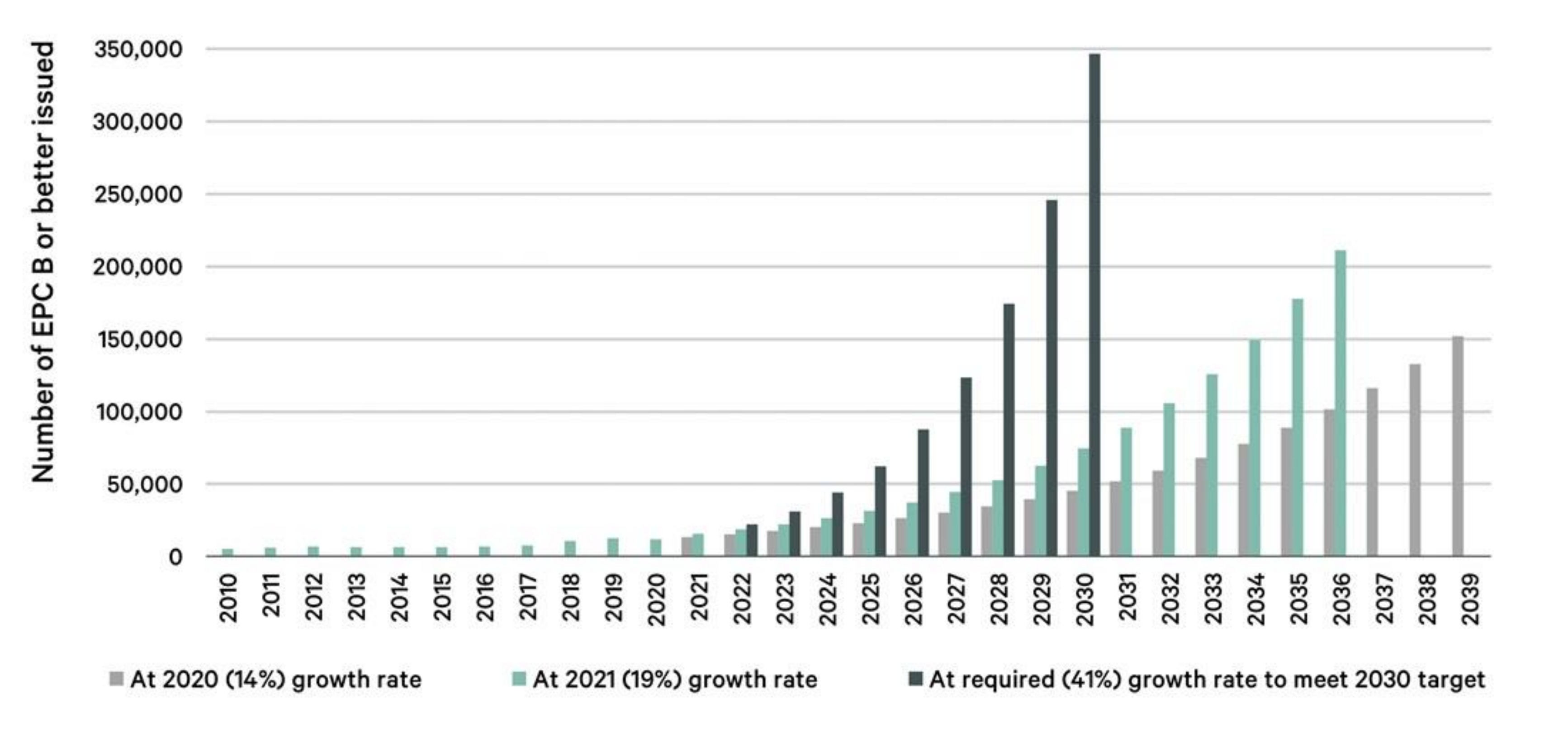
- 1 April 2018 – new commercial leases require EPC rating of at least E
- 1 April 2023 – it becomes an offence to continue to let commercial property with an EPC rating below E unless specific exemption applies
- 1 April 2030 – proposal for minimum EPC rating of B for all commercial property.

<u>Factors for consideration</u>

- Possible works required to improve energy efficiency and question who pays for the works?
  - Service charge v improvement to the building
  - Access arrangements
- Who enforces for breach and what does it mean
  - Fine by the Local Authority against the landlord of between £5,000 - £150,000.

Heat & Building Strategy, UK Green Taxonomy and Sustainability Disclosure Requirements

CBRE forecast re EPC of C or above in 2030



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What does a property strategy look like?

Property as a tool for change

Property strategy born out of the current market, projected trends and business needs.

2 key elements of a strategy are therefore:

Managing property costs effectively	Using your property to support your ESG agenda

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Managing property costs

Action	Lease clauses	Considerations
Move	Alienation provisions Break right Yielding up and repair obligations	Continuing liability Dilapidations
PPM	Repair and decoration Alterations Service charge	Restriction on dilapidations claims
Monetise lease event	Break	Flexibility in the future
Reduce space	Alienation and sharing provisions	Continuing liability Costs of dividing premises
Reduce cost of utilities	Alterations Service charge provisions	ESG agenda

Environmental aspects of ESG

Action	Lease clauses	Considerations
Net zero	Service charge Alterations Yielding up	Can this be done alone? Cost benefit analysis for this property
Implement wellness programme	Service charge Alterations Yielding up	Cost benefit analysis for the property
Retro fit	Demise Service charge Alterations	Repair v improvement

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Social aspects of ESG

Action	Lease clause	Consideration
Implementing flexible working	Demise Alterations	Staff engagement Landlord's consent? Cost of works
Wellness programme	Demise Service charge	Staff engagement HR policy
Creating a destination office	Demise Alterations	Business plan HR policy

Governance aspects of ESG

Action	Lease Clause	Consideration
Plan and implement a sustainable property strategy	The Lease	Your lease HR policy Business plan Trustees duties Internal stakeholder views

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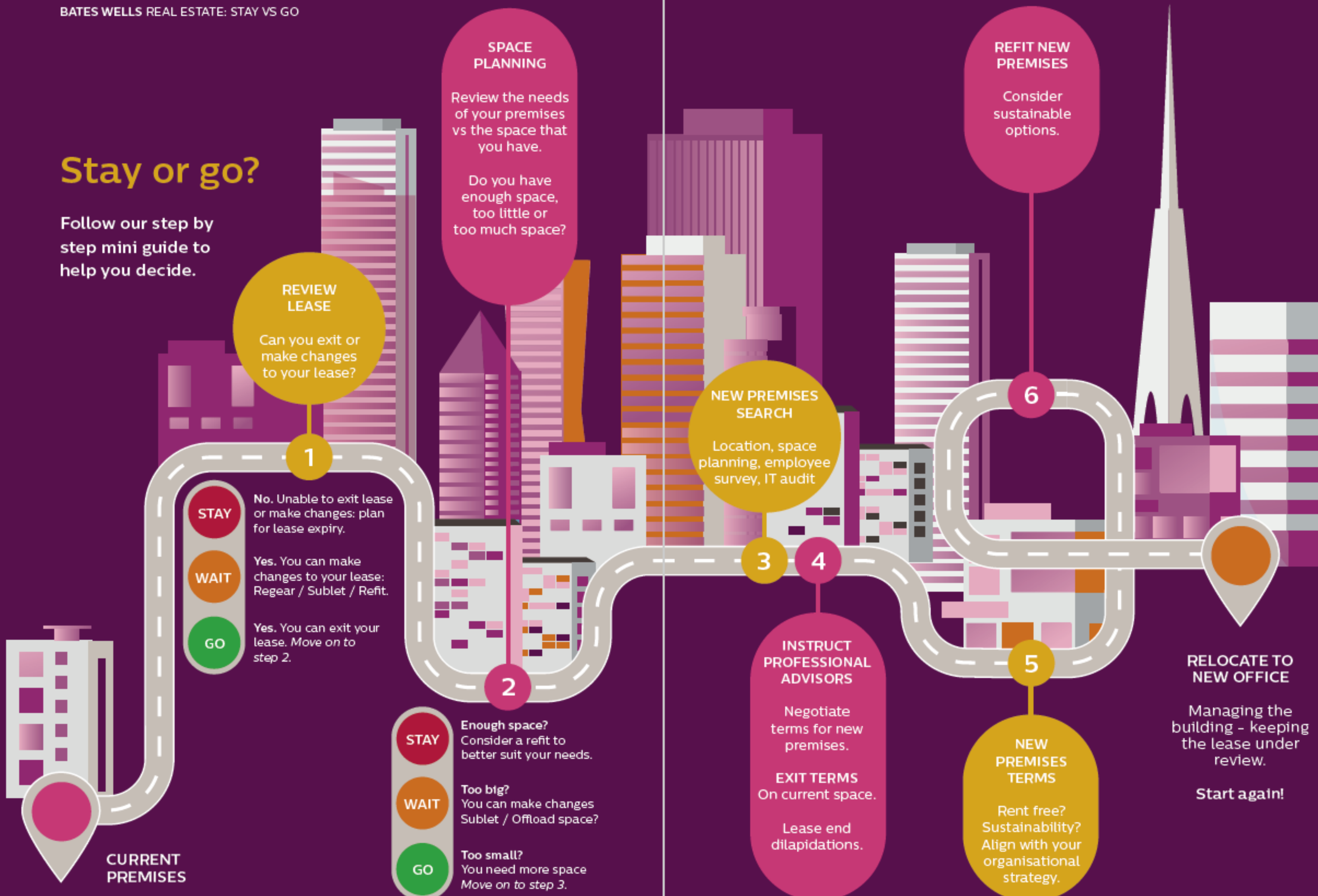
Stay or go?

Follow our step by step mini guide to help you decide.



Property life cycle: the benefits of an impact driven cycle

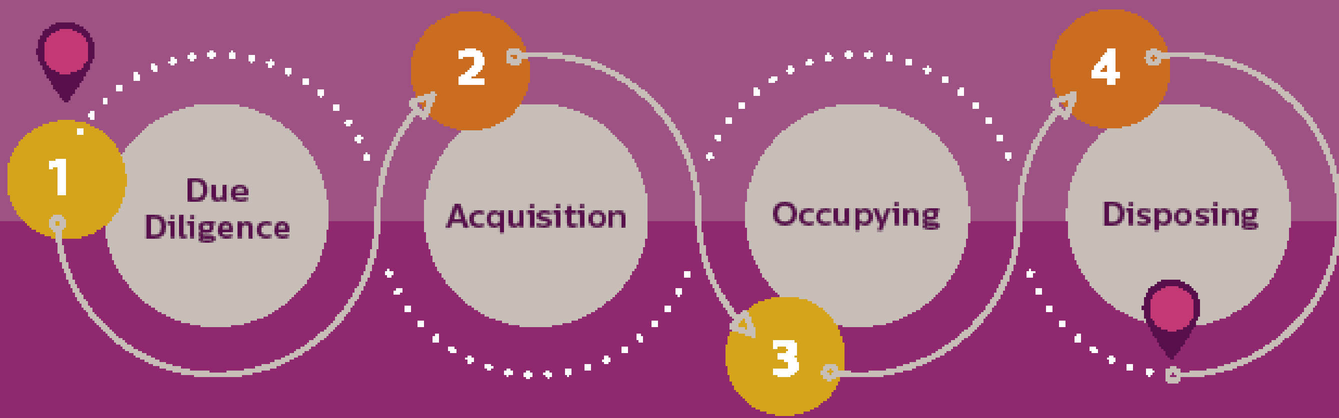
Standard property life cycle:

- Site identification
- Financing
- Surveys and searches

- Purchase of freehold or long leasehold/taking a lease
- Initial works

- PPM
- Usual division of landlord and tenant obligations

- Disposal mechanism: stay vs go, income generating asset
- Dilapidations



Enhanced impact driven life cycle:

- Accreditation
- Emissions
- Waste management
- Space planning

- Sustainable fit-out biophilic design
- Sustainable finance

- Community driven sustainable occupation
- Increased health and wellbeing
- Reduced emissions
- Cost savings

- Environmental costs
- Circular economy factors
- UN sustainable development goals

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Potential benefits of following the impact 'enhanced' life cycle are:

- Environmental
- People (attracting and retaining talent)
- Long-term cost reduction
- Improved investor confidence
- Reputational

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How might your sustainable property strategy impact your financing arrangements?

Sustainable / ESG financing – setting the scene:

- Huge growth in ESG investment and lending in the financial markets over the last 10 years
- What does ESG investment actually mean for lenders / investors?

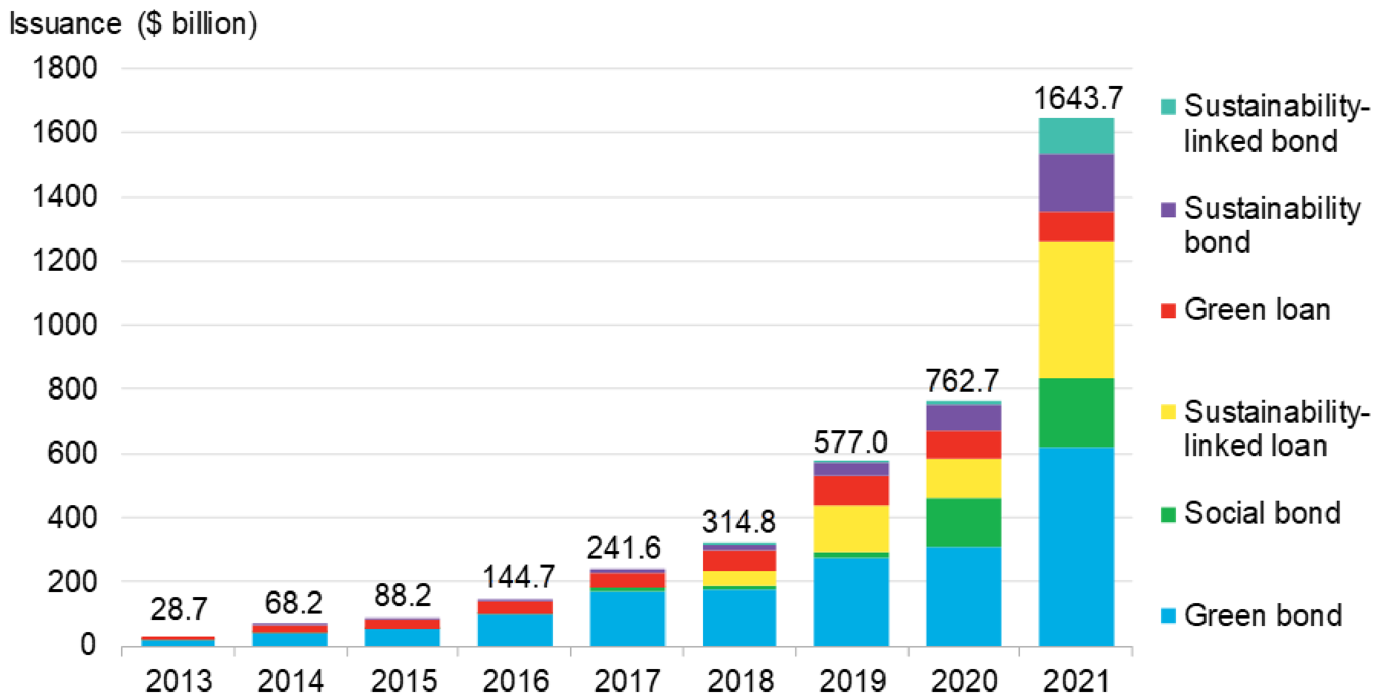
  "Obtaining a long-term financial return by understanding and using ESG factors to <u>reduce long-term risks</u> and identifying <u>long-term growth opportunities</u>"

- What does this look like in practice?
  - **Firstly**: development and growth in new ESG investment products:
    - **Green loans and bonds** – funding proceeds can only be applied towards certain "green projects", such as "greening" new or refurbished buildings e.g. increasing energy efficiency / waste reduction strategies / retrofit works / improved water consumption etc.
    - **Social loans and bonds** – funding proceeds applied towards certain "social projects" such as essential services, affordable housing and food security
    - **Sustainability-linked loans and bonds** – funding proceeds can be used for general corporate purposes; the borrower's interest rate can go up or down depending how they perform on pre-agreed ESG targets (which could include sustainable property targets)
  - **Secondly**: lenders and investors adapting their existing credit risk / due diligence processes to reflect ESG measures such as your sustainable property strategy

Annual growth in ESG investment products

Significant growth (globally) over the last ten years – from $28.7 billion in 2023, to $1.65 trillion in 2021:

Figure 1: Annual sustainable debt issuance, 2013-2021



Source: BloombergNEF, Bloomberg L.P.

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How does this apply to charities?

If you are a charity looking for ways to **fund** the "greening" of your existing (or future) propert(y)/(ies), the growth of the mainstream **green loans** market may be a useful avenue to explore:

Key features of green loans include

Feature	Comments
Use of Proceeds	Must be used for "Green Projects" – no legal definition; each lender will have their own criteria. There are increasing discussions around what constitutes a "green building". The World Green Building Council defines this as: "*a building that, in its design, construction or operation, reduces or eliminates negative impacts, and can create positive impacts, on our climate and natural environment*". For green loans, permitted use of funds will generally include funding for improving energy performance and water consumption, as well as other spending which contribute to climate change mitigation or other environmental goals (i.e. retrofit works).
Process of project evaluation and selection	Borrowers will be asked to provide: (1) details of the green project, (2) how the loan amounts will be allocated, (3) the expected environmental impact, and (4) how they will identify and manage potential environmental risks.

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Green loans cont'd

Feature	Comments
Process of project evaluation and selection (cont'd)	The Lender or an external party may ask to verify this – there is a growing body of standards and certifications that help to determine the "greenness" of a particular project, or property, such as: • EPCs • Alignment to the EU Taxonomy (or other recognised taxonomies) • BREEM New Construction / Refurbishment & Fit-out • LEED Certification
Management of proceeds	Lenders will usually ask that the loan proceeds go to a dedicated bank account, or be tracked by the borrower to maintain transparency
Reporting	Borrowers will need to provide annual (or more frequent) reports on how the loan proceeds have been used, as well as "green" impact achieved – potentially against pre-agreed metrics e.g. energy capacity / electricity generation / greenhouse gas emissions reduced etc. Also any exceptions, controversies and mitigating actions, if applicable.

The LMA (Loan Market Association) provides excellent further guidance on the key features of green loans for real estate projects:
https://www.lma.eu.com/application/files/2316/0552/7456/01_LMA_Case_Study_REF_Investments_Green_Buildings_V06.pdf

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Sustainable finance – other considerations

Sustainability-linked loans:

- To recap, funding proceeds can be used for general corporate purposes; the borrower's interest rate can go up or down depending how they perform on pre-agreed ESG targets (which could include sustainable property targets)
- May involve wider scrutiny of charity's wider ESG performance e.g. governance / employee relations / supply chains etc. – not just property sustainability.
- May be useful if the charity wants a prompt to boost its ESG performance more widely, in any case.

General lending and ESG metrics:

- Even if you are not looking to borrow specific ESG investment products, there is an overall trend towards more lenders increasingly focusing on their borrowers' ESG metrics
- Greater scrutiny of the lenders' own ESG performance – and increasing current and future regulation in the investment space
- New general lending / refinancings – particularly for real estate financings; ESG metrics we have been discussing may form a greater part of lenders' due diligence and credit risk processes
- Challenges of proportionality – especially for smaller charities / borrowers
- Do speak to your lenders about what this might mean for you: upcoming challenges – as well as opportunities!

Any questions?

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