

ACC Charlotte Chapter

Green Leases and Sustainability Peter McLean, Partner

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www.klgates.com

WHAT IS “GREEN”?

- Google Search – 2,170,000 results
- Definitions
- Slang Usages
- Modern Use – “Environmentally Friendly”

WHY GO “GREEN”?

- Historically
 - “Save the Planet” Extremism
- Now
 - Still “Save the Planet”
 - Economic Benefits

WHAT MAKES A BUILDING/SPACE “GREEN”?

- Energy Usage
 - HVAC/Lighting
- Water Usage
- Indoor Air Quality (“IAQ”)

WHAT MAKES A BUILDING/SPACE “GREEN”?

- Reduction of Energy Consumption
- Reduction of Potable Water Usage
- Improve IAQ

WHY DO WE CARE?

- USGBC reports that:
 - Buildings annually consume more than 30% of total energy and more than 60% of electricity used in the U.S.
 - 5 billion gallons of potable water used daily solely to flush toilets

WHAT CONSTITUTES A “GREEN” LEASE?

- No established criteria
- Building and space “certifications” (LEED, GreenGlobes, Energy Star) have led to the necessity of new lease language
- Lease sets forth the “rules” for construction/operation and maintenance of the space

WHY A “GREEN” LEASE?

- Must make economic sense
- Add value to the Landlord’s business
 - Increase rental rate
 - Increase occupancy rate
- Add value to Tenant’s business
 - Lower rent costs
 - Improve operating conditions for personnel
- Economically contradictory incentives

MAKING A “GREEN” LEASE WORK

- Must make both Landlord and Tenant happy
- Conquer the “split-incentive”
 - Who pays and who benefits?

“GREEN” LEASE SPECIFICS –INITIAL CONSIDERATIONS

- What “shade” of “green” is desired?
- How do you reach objectives?
- Will some official “certification” be pursued?

HOLISTIC APPROACH

- Establish specific objectives and goals
- Communicate to entire “team”
- Site selection
- RFP
- LOI
- Lease

EXAMPLES OF LEASE PROVISIONS AFFECTED

- Most are apparent
- Some more subtle
- Dependent on objectives/goals

“LEGAL” CONCERNS – LIABILITY TRAPS

- What can you promise?
- Who is responsible for what?
- Construction contracts
- Architect contracts
- Consultant agreements

CORPORATE SUSTAINABILITY

- Rule #1: Green = Gold
 - Peripheral issues nice, but must follow rule #1

GREEN LEASE RESOURCES

- Green Office Guide: Integrating LEED into Your Leasing Process – US Green Building Council (USGBC), 2009 (tenant oriented) (www.usgbc.org)
 - Comprehensive manual designed to assist tenants green the leasing process
 - Addresses site selection, negotiations, lease language, build out, ongoing operations
- Lease Guide: Guide to Writing a Commercial Real Estate Lease – Building Owners and Managers Assoc. Int. (BOMA), 2008 (landlord oriented) (www.BOMA.org)
 - Form of commercial lease agreement that includes green provisions

GREEN LEASE RESOURCES

- Green Lease Guide for Commercial Office Tenants – Real Property Association of Canada (REALpac) (2010) (www.realpac.ca)
 - Manual designed to provide information to assist tenants and is a companion to the REALpac “Office Green Lease” National Standard Lease for Single-Building Projects

QUESTIONS?

peter.mclean@klgates.com

704.331.7421 TEL

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www.klgates.com

Author:**Martin E. Garza**

martin.garza@klgates.com

+1.214.939.5802

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LEED for Healthcare Moving Towards Full Launch

The U.S. Green Building Council (USGBC) is poised to fully implement the LEED for Healthcare rating system as part of its Leadership in Energy and Environmental Design (LEED®) program. USGBC's LEED program promotes and recognizes sustainability and better environmental and health practices throughout the design, construction and operation of a project. USGBC members voted with an 87% approval rate in November 2010 for LEED for Healthcare. USGBC expects to fully launch the LEED for Healthcare rating system in Spring 2011.

LEED for Healthcare presents an opportunity for those in the healthcare sector who may have waited on the sidelines to commit to a LEED initiative under the existing rating systems. The LEED for Healthcare rating system will provide opportunities for a variety of medical and healthcare facilities, including the following:

- licensed and federal inpatient, outpatient and long-term care facilities;
- unlicensed outpatient facilities;
- medical offices and clinics;
- dental offices and clinics;
- veterinary offices and clinics;
- assisted living facilities; and
- medical education and research centers.

The development of this new rating system has been under way for some time. As the USGBC notes:

LEED for Healthcare is designed to guide and distinguish high-performance healthcare projects, including inpatient and outpatient care facilities and long term care facilities.

The LEED for Healthcare rating system represents a culmination of seven years of close collaboration between the Green Guide for Healthcare (GGHC) and USGBC. GGHC has helped to streamline the LEED for Healthcare's development schedule by aligning with the LEED for New Construction rating system's organizational structure, with permission from USGBC, and conducting a robust pilot program that has included more than 100 health care facilities.

The GGHC pilot project informed the development of the LEED for Healthcare rating system. The combined efforts have specifically addressed the usability and verifiability of the draft credits, with feedback solicited from the pilots on their use of the GGHC. This has made it possible to bypass the pilot process with LEED for Healthcare. When approved by USGBC membership, all healthcare projects will have access to the rating system, including the reference guide, workshops, and LEED Online¹.

Many of the core concepts of LEED, including reducing exposure to chemicals and pollutants, improving indoor air quality, and creating healthier and more productive work environments, align particularly well with the universal medical industry goals of healing, medical treatment and disease prevention. Although there are a number of similarities between LEED for Healthcare and LEED for New Construction, LEED for Healthcare also addresses issues that are unique to the healthcare industry. For example, many medical facilities operate around the clock, seven days week, while retail and office space are subject to typical business hours on applicable business days. Additionally, healthcare facilities are subject to regulatory requirements that are not imposed on typical office or retail space, such as infection control, waste disposal and patient privacy. In order to meet these unique needs, the USGBC points out that 6 prerequisites and 25 credits were modified (as compared to LEED for New Construction), and 3 new prerequisites and 15 credits were added in the LEED for Healthcare rating system. The minimum program requirements which apply to LEED for New Construction also will apply to LEED for Healthcare.

As with any program, and especially for new concepts that are being put to the test for the first time, it is important to recognize and understand the legal issues that may be presented by the LEED for Healthcare rating system. A variety of parties may be involved at any point during the life-cycle of the project, including architects, engineers, contractors, vendors, lenders, and tenants. If expectations, obligations or goals are not met, who will bear the associated risk and responsibility, And what remedies will be available for any such failure?

In this ever-changing environment, clients should examine how green programs might impact their operations, facilities, strategy and investments. With 50+ LEED Accredited Professional (LEED®-AP) lawyers, along with the extensive real estate, land use, tax and healthcare experience of these and other lawyers in the firm, K&L Gates is positioned around the globe to advise clients as they navigate the opportunities green initiatives and sustainable development may provide to their businesses and bottom lines.

Martin E. Garza is a real estate and land use partner in the Dallas, Texas office of K&L Gates. Martin is a LEED®-AP and Texas REALTOR®. Martin's biography is available via www.TexasLEEDLawyer.com.

¹ <http://www.usgbc.org/DisplayPage.aspx?CMSPageID=1765>

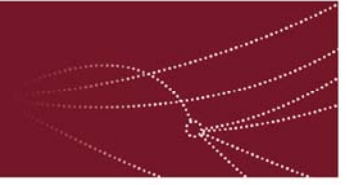
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www.klgates.com**Authors:****Steven Cox**

steven.cox@klgates.com
+44.(0)20.7360.8213

Bonny Hedderly

bonny.hedderly@klgates.com
+44.(0)20.7360.8192

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IPD Sustainable Property Index (ISPI)

K&L Gates, through its London Office, has agreed to be co-sponsor of a new commercial real estate index in the UK called the IPD Sustainable Property Index (or ISPI for short). In the United States, research has shown that energy efficient buildings can command higher rents and capital values than less efficient buildings, but in the UK there has been only limited corresponding research. This means that whilst many fund managers feel instinctively that sustainable buildings are a better investment because they should be more attractive to tenants in terms of lower running costs, less danger of obsolescence, improved indoor air quality etc, there is no hard data to support this view. Until there is this data, valuation professionals are reluctant to reflect sustainability in valuations. One of the sources of this data for the future will be ISPI, which therefore means it will be likely to play a significant role in investment decision-making in the future.

What it is and how it works

ISPI is the only sustainable property investment index produced anywhere in the world. ISPI is produced by IPD - Investment Property Databank - which is the world's number one provider of in commercial real estate performance analysis and indices for the owners, investors, managers and occupiers of real estate. It operates in over 20 countries including most of Europe, the US, Canada, South Africa, Australia, New Zealand and Japan. The other sponsor is an industry body called the Investment Property Forum (IPF) which is a leading industry group in the UK providing research, education and networking opportunities for fund managers, analysts and other real estate professionals. Over 60 funds have so far provided data to ISPI.

According to the methodology used to compile the index, buildings that achieve a high rating with LEED, BREEAM and similar systems are automatically treated as "more sustainable". Buildings that are not certified under one of these systems are analysed by environmental criteria such as energy, water, waste, flooding, building quality and accessibility. The sustainability of each property is linked to its financial performance to see whether the more sustainable properties achieve better returns than the less sustainable properties. This will enable investors to measure the impact of sustainability on the investment performance of their portfolios.

ISPI has been created in the UK and could easily be replicated globally. Indeed, IPD consider that Australia, Canada and Germany are already "market-ready"

Looking ahead with ISPI

Christina Cudworth, Head of Sustainability at IPD, said: “The UK property industry is clearly only just at the beginning of a long and gradual process in which occupiers start to base their property decisions on the sorts of sustainable investment, location and management practices which are captured in the ISPI Consultative Release methodology. Understanding and measuring the relationship between sustainability and investment performance is a critical priority for the property industry. As occupiers increasingly factor sustainability metrics into their decision making, a clearer performance division between more and less sustainable properties will undoubtedly emerge. ISPI will capture that performance differential as practices in this area mature.”

Wayne Smith, Head of Real Estate in the London Office of K&L Gates, said: “ISPI is a unique product, and we are delighted to be aligned with the IPF and the IPD in supporting ISPI. As an international law firm, with a worldwide sustainability practice, ISPI is a perfect fit for us, especially given the interest and support afforded to this product by some of our core real estate fund clients.”

If you would like any further information about ISPI please feel free to contact Steven Cox or Bonny Hedderly. For further information on IPD, visit www.ipd.com.

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For Better or Worse: White House Proposes Better Buildings Initiative

President Obama has proposed new efforts to make commercial buildings more efficient through his “Better Buildings Initiative” (BBI). The BBI includes a variety of tools, including tax incentives, loan guarantees, streamlining of regulations and other measures, to further energy efficiency in buildings. If these initiatives move forward, owners and managers of offices, stores, schools, municipal buildings, universities, hospitals, and other commercial buildings may be looking at energy saving upgrades to their facilities. Some industry groups are beginning to line up in support of this initiative, while others may be less than enthusiastic about how such measures would be adopted and implemented.

Outline of the Better Buildings Initiative

According to the White House, in 2010 commercial buildings consumed roughly 20 percent of all energy in the U.S. economy. The Environmental Protection Agency estimates that about 30 percent of energy in buildings is used inefficiently or unnecessarily. Improved energy efficiency in buildings can “create jobs, save money, reduce our dependence on foreign oil, and make our air cleaner,” claims the White House.

The goals under the BBI include: (1) achieving 20 percent improvement in energy efficiency by 2020; (2) reducing building owner and company energy expenses by about \$40 billion per year; and (3) stimulating the private sector and local and state governments to work toward the President’s energy efficiency goals. Some of the initiatives proposed to support these goals include:

- changing the current tax deduction for commercial building upgrades to a tax credit for qualifying energy efficient upgrades
- promoting the use of increased loan limits for energy efficiency retrofit loans through the Small Business Administration and existing lenders
- providing competitive grants to state and local governments that “streamline standards, encouraging upgrades and attracting private sector investment” in what the White House calls a “Race to Green”
- challenging universities and private companies through the “Better Buildings Challenge” to actively support and promote energy efficiency goals and programs in the private sector (former president Bill Clinton, and Jeff Immelt, CEO of General Electric, have been asked to co-lead this effort)
- implementing new reforms to encourage and improve training in building operation technologies and energy efficiency

Reaction from Industry Groups

Reaction from commercial industry groups has been generally supportive. The Building Owners and Managers Association (BOMA) International has come out in support of the BBI, saying it “dovetails with BOMA International’s long-term commitment to helping building owners and managers reduce energy use by promoting energy management practices through a variety of platforms.” The National Multi Housing Council and the National Apartment Association also endorsed the BBI and its financial incentives for making structures more energy efficient. The U.S. Green Building Council (USGBC), the non-profit organization which established the Leadership in Energy and Environmental Design (LEED) green building certification program, has also endorsed the President’s plan.

Will the Better Buildings Initiative Take Hold?

While it is far too early to see whether the BBI will take hold, there are a variety of factors for building owners and businesses to consider if and when aspects of this initiative come to fruition:

LEED Certification:

The stick and carrot of heightened local regulations and financial incentives may provide extra incentives for building owners to not only upgrade existing buildings, but to seek out LEED certification in the process. The LEED green building program is a certification program which recognizes projects that implement strategies to promote sustainability, reduce environmental impacts and improve energy efficiency, among other things. According to the USGBC, over 40,000 projects are already participating in the commercial and institutional LEED rating systems. The USGBC highlights certain benefits in making the business case for green building certification: competitive differentiation, risk mitigation, attractiveness to tenants, cost effectiveness, and increased rental rates.¹ Getting there, however, has its costs in meeting design, planning, construction, and other requirements in order to obtain LEED certification.

¹ <http://www.usgbc.org/DisplayPage.aspx?CMSPageID=2331>

Heightened State and Local Regulations:

Building owners and developers will need to keep a close eye to see how the “Race to Green” impacts state and local laws and their wallets. Even before BBI, an increasing number of green legislative proposals have been making headway around the country. For example, a measure before the New Jersey Assembly would require electric vehicle charging stations at new shopping centers. The goal is to have infrastructure in place at shopping centers and rest areas around the state to recharge electric vehicles. Charging units reportedly cost about \$6,000 apiece. Another measure would require at least 5 percent of the parking facilities at shopping centers to include charging stations. At least one official with the International Council of Shopping Centers (ICSC) has some objections to the proposed New Jersey legislation stating:

We support the intent of the legislation to improve the environment and provide a service to consumers, but we disagree with the premise, which is a requirement for only shopping centers. ...The same requirement isn’t applied to other types of property, such as hotels or offices or hospitals. It is shopping centers only, and that is inequitable.²

Questions of equity, timing, and costs will be among the variety of issues discussed as state and local laws are proposed and adopted. Will benefits be offered, such as tax credits, accelerated permitting, or financing options, to offset the costs? Is the technology ripe for implementation, or should the market help decide rather than the government? If LEED-type standards are required by law, are they attainable? Building owners may need to take a more active role on a state and local basis in key markets where new green regulations are being considered.

Timing of Upgrades:

What impact does the BBI announcement have on timing and implementation of planned upgrades for building owners? Does it make sense to wait to see if BBI pans out and new tax incentives are made available? Or is it better to invest in upgrades now

² http://www.icsc.org/apps/news_item.php?id=2733

to capture energy cost savings earlier or to vest certain rights under current regulations? Although this is a national initiative, these decisions may need to be made on a site-by-site basis depending on local regulatory, political, business, and market conditions.

In this ever-changing environment, clients should examine whether green incentives and policies might impact their operations, site selection, strategy and investments. With 60+ LEED Accredited Professional (LEED®-AP) lawyers, along with the real estate, land use, tax and governmental

experience of these and other lawyers in the firm, K&L Gates is positioned around the globe to advise clients as they navigate green initiatives and sustainable development programs that could impact their businesses and bottom lines.

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Peter McLean III

CHARLOTTE OFFICE

704.331.7421 TEL

704.353.3121 FAX

peter.mclean@klgates.com

AREAS OF PRACTICE

Mr. McLean is a partner in the Charlotte office and his practice is focused on real estate development with an emphasis on commercial leasing. He has extensive experience in negotiating and preparing a wide variety of complex office, retail and industrial leases, ground leases and build-to-suit agreements, both in the context of stand-alone and mixed-use developments. During the course of his career, he has been involved in virtually all phases of commercial real estate acquisitions, development, leasing, sales and financing activities.

Mr. McLean is a LEED Accredited Professional (LEED-AP), a distinction he earned through the Green Building Certification Institute. As a LEED-AP, he has demonstrated a thorough understanding of green building practices and principles, as well as the LEED Rating System.

PROFESSIONAL BACKGROUND

Prior to law school, Mr. McLean was a Lieutenant in the United States Navy, serving from 1971-1978.

PRESENTATIONS

- Speaker at North Carolina Bar Association Real Property Section Meeting- Commercial Real Estate Leasing
- Panelist for USGBC Charlotte Region Chapter program – “LEED In The Real World”
- Faculty Panelist at the Charlotte Symposium regarding the “Green Lease Revolution”, discussing the Model Green Lease and issues surrounding Green Leasing and related sustainability initiatives

PUBLICATIONS

- “The Importance Of Use Provisions In Retail Leases,” *North Carolina Lawyers Weekly*, July 2003

BAR MEMBERSHIP

North Carolina

EDUCATION

J.D., Wake Forest University, 1981 (*cum laude*; Managing Editor, *Wake Forest Law Review*)

A.B., Dartmouth College, 1971

ACHIEVEMENTS

- *Best Lawyers in America*, Real Estate Law, 2009-2011
- *North Carolina Super Lawyers*, Real Estate Law, 2006

REPRESENTATIVE EXPERIENCE

- Represented owner/developer in connection with all aspects of the acquisition,

development, financing, leasing and sale of an approximately 600,000 square foot retail facility.

- Represented owner/developer in connection with the assemblage and acquisition of land from 20+ property owners and the subsequent development of a 1.4 million square foot regional retail facility.
- Represented developer in connection with the negotiation and leasing of an 800,000 square foot multi-building office "campus" facility.
- Represented foreign-owned corporation in the lease and development of its North American headquarters and manufacturing facility, including assisting with various state and local incentive agreements.