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Group Contact:

Barry Trilling, Partner
203.363.7670
btrilling@wiggin.com

About the Climate Change and Sustainable Development Group

No area of our economy – manufacturing, resource production, real estate, construction, transportation, technology, or investment and finance – can fully avoid confronting the newly emerging regulatory and business initiatives on climate change and sustainable development. These developments have affected the clients of almost every practice group at Wiggin and Dana and although we cannot predict the full scope of the new paradigm that will emerge, it will certainly include efforts to ameliorate climate change by reducing pollution, developing new technologies, and changing corporate practices. These efforts will, in turn, create both new opportunities and challenges for our clients and how our law firm represents them.

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The Economics of Green Building: The Developer's Perspective

Barry J. Trilling, a partner at Wiggin and Dana, LLP and Chair of the firm's Climate Change and Sustainable Development Inter-Disciplinary Practice Group, delivered the following remarks on February 29, 2008, at the University of Connecticut School of Law's 15th Gallivan Conference on sustainable development. Mr. Trilling also currently serves as Chair of the Government and Legislative Affairs Committee of the New York City/Westchester County/Fairfield County Chapter of the National Association of Industrial and Office Properties (NAIOP), is the immediate past president of that chapter, and a member of NAIOP's national Urban Redevelopment Forum.

According to a November 2007 article published by the RREEF Research Foundation, "Buildings account for 39% of the *nation's* primary energy use, 70% of its electricity consumption, 30% of raw materials use and 30% of greenhouse gas emissions." At a June 2007 program sponsored by the New York City Bar and the Pace Law School Land Use Center entitled "Creating Profitable and Sustainable Urban Developments," Stephen B. Siegel, Global Chair of CB Richard Ellis (CBRE), the world's largest commercial real estate services company managing 1.7 billion square feet of building space, noted that today's buildings account for 12% of the *world's* water use, 40% of the world's greenhouse gas emissions, 65% of the world's waste output, and 70% of the world's electricity consumption. CBRE's reaction: it is "going green." The company has adopted a goal to become carbon neutral by 2010 at the more than 5 million square feet it occupies worldwide through a combination of energy savings, more efficient space utilization, carbon emissions reductions and, if necessary, investments in carbon offsets. The real estate development industry is as aware as any part of the commercial sector that, without reduction of our carbon footprint, we can anticipate the disastrous consequences of global climate change. These include rising shorelines, reductions in agricultural productivity, and more intense and frequent weather incidents. As with industry leader CBRE, the commercial real estate community is widely adopting development strategies that are part of the solution and is reacting productively to the pressures caused by climate change and the need for sustainable development.

The momentum for "greening" real estate development has steadily grown for almost a decade. In the initial stages of the green building movement, public and corporate sector entities—rather than real estate owners, developers, and investors—took the lead. These public and corporate entities, which consume large areas of office space, frequently constitute either owner-users or single tenants who are better situated to capture the benefits of green development than the owners of smaller or multi-tenanted properties. Traditional property owners frequently operate on a "net-net basis," meaning that the tenant bears the burden of taxes and utility costs. Hence the tenant, rather than the owner, reaps the benefit of energy efficiency. Further, these larger space users have more immediate sensitivity to increases in worker productivity that accompany green development.

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Today, however, the dynamics have substantially changed—although the public and corporate sectors continue to dominate the demand for and construction of green buildings. Factors such as tenant demand, governmental mandates, corporate accountability, socially conscious investment vehicles, and financial pressure exerted by traditional capital providers (both equity and debt) have resulted in a “greening” trend that will redefine Class A office space. Already in New York City, the market does not recognize a new building as Class A space unless it meets a “green standard.”

The demand for sustainable design features and seemingly endless escalation of energy costs, along with both government mandates and government incentives, will drive increased participation in green development by commercial real estate’s owners, investors, and developers. A heavy-handed intrusion by governmental entities, however, including cookie-cutter solutions to differing problems imposed from above, threatens to inhibit rather than advance green development. Some combination of green-sensitive code requirements and incentives to build and lease green buildings, on the other hand, should prove more effective in encouraging this green development trend.

We already see the market encouraging this trend. In major urban markets, particularly the New York and Boston metropolitan areas, almost all new major construction is at least partly green, and much of it achieves the highest of currently recognized standards. We should continue to see market pressures moving developers to build green in other urban areas. Market incentives for more green development include evidence of energy savings that average 30% less than conventional buildings, amounting to an annual savings of \$135,000 for a typical 200,000 square foot building. Larger problems confront us with regard to renovation and rehabilitation, which raise issues of cost and feasibility that do not confront new construction. The November 2007 RREEF article put it this way:

“For new construction, the emerging consensus is that with careful planning, the cost premium for green construction can be minimal to non-existent, and well within the normal range of early-stage cost contingencies; from there, cost reductions through value-engineering often bring down projected premiums when the building is actually constructed. Green buildings are also eligible for a variety of incentives that can more than offset any putative cost premiums.

“The costs and net benefits of renovating existing buildings to green standards is less certain because the extreme diversity of the standing stock (e.g. age, condition, quality) makes blanket statements impossible.”

Without some external incentive, such as expedited permitting or government subsidy to either developer or tenant (via tax break or otherwise), the market is not likely to favor green renovation, at least until the capital expense savings resulting from the renovation meet or exceed the renovation costs. Programs to compel all renovation to meet government imposed standards are thus likely to result in the absence of renovation and a deteriorating, less energy-efficient building stock.

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The creation and acceptance of national standards, which have been adopted for the most part on a voluntary basis, have also moved the ball forward for green development of commercial and industrial office space. These standards include the U.S. Green Building Council's Leadership in Energy and Environmental Design (LEED) rating system, the Green Globes USA design program of the U.S. Green Building Initiative, and the energy standards set forth in the American Society of Heating, Ventilating and Air Conditioning Engineers (ASHRAE) Standard 90.1. These standards all set uniform goals that commit discussion of these issues to a common vocabulary.

The LEED standard, for example, stresses energy efficiency, but also includes sensitive land use, conservation of natural resources, and prudent but comfortable indoor conditions. The LEED program has separate levels (certification, silver, gold, and platinum) and different standards that apply to new construction, renovation, and interiors. The U.S. Green Building Council is now working with my trade association, the National Association of Industrial and Office Properties, to develop a standard for warehouse and other distribution facilities.

As demonstrated in the New York and Boston markets, green buildings fill up with tenants more quickly than their conventional counterparts, bring in higher rents, and maintain their occupancy levels longer than buildings that are not green. These developments in the market have been accomplished by voluntary action, rather than effort compelled by government mandate. The market has been able to adapt the need for particular kinds of green development to suit particular developmental, community, and climatic needs.

Notwithstanding the benefits of voluntary action and the influence of the free market, some mandatory green programs are appropriate and well thought out. For example, it makes sense for local building codes to reflect energy efficiency requirements and smart land use. In addition, a local approach is most sensitive both to ecological and development needs. Using this approach, more than 65 local governments in the United States have made a commitment to LEED standards in building construction, while others have trimmed the entitlement process and offered tax credits to spur green development. Overarching federal and state solutions, however, imposed without consideration of the effect on local needs or the intricacies of the development process do not appear advisable.

A good example of a bad solution appears right here in Connecticut with changes to the Connecticut State Building Code mandated in Public Act 07-242, enacted in June 2007. Added as a last minute insertion without the benefit of public participation, Section 78 of the statute requires the private sector to meet the LEED silver standard or its equivalent for (1) buildings costing \$5 million or more built after January 1, 2009 and (2) renovations costing \$2 million or more starting January 1, 2010. Those requirements apply to projects other than residential buildings with up to four units. Although these requirements may be waived if the Institute for Sustainable Energy finds that the cost of compliance significantly outweighs the benefits, these changes to the State Building Code would result not only in increased cost and delays, but also potentially in litigation and the disincentive to build in Connecticut rather than in neighboring states.

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Moreover, Public Act 07-242 and the code amendments that have been proposed to implement that statute leave open many important questions. For example, the act and code amendments do not define what constitutes renovation for the purpose of the requirement to utilize the LEED standard, nor do they provide any guidance on how to calculate threshold amounts. It is unclear, therefore, whether these amounts include expenses for environmental remediation or the cost of installing energy efficient materials. Uncertainty also results from an absence of guidance as to what constitutes equivalency to the LEED silver standard. For example, will accommodations be made to recognize differing climate conditions unique to Connecticut? Will the new requirements differentiate among office, warehouse, industrial, and multi-family properties, all of which require differing construction techniques? Other crucial questions abound: What will happen if LEED certification or an equivalency determination is delayed or denied? Will this delay or denial result in the refusal to grant a Certificate of Occupancy or a penalty? What standards will the Institute for Sustainable Energy use to determine whether the cost of compliance significantly outweighs the benefits? What procedure will the Institute use to assure due process to the parties whose livelihoods will be affected by those determinations?

Imprudent answers to these questions could result in unjustifiable, potentially unconstitutional deprivations of property and ensuing litigation. Another result could be the inhibition of both new construction and much needed renovation that keeps our Connecticut building inventory safe, productive, and energy efficient. This inhibition could have a particularly harsh effect on the redevelopment of Brownfield properties, which already suffer from the disadvantage of the need to clean up historical contamination.

A more sensible solution was proposed in the General Assembly in the form of Raised Bill 5798 which would establish a tax credit for real estate projects that meet or exceed LEED silver certification.

We should keep in mind the old warning about where the path leads that is paved with good intentions, or to mix metaphors, remain aware of the law of unintended consequences. In so doing, we should recognize that green development makes sense for everyone—communities, government, owners, developers, investors, tenants, as well as for the climate and the environment. Government, communities, green development advocates, and the real estate development community need to work together to assure that we can meet our common goals for sustainability in a sensible, productive manner that considers the needs of all stakeholders.

The Wiggin and Dana Sustainable Developments e-Newsletter is a periodic newsletter designed to inform clients and others about recent developments in the field of climate change and sustainable developments law. Nothing in the e-Newsletter constitutes legal advice, which can only be obtained as a result of personal consultation with an attorney. The information published here is believed to be accurate at the time of publication, but is subject to change and does not purport to be a complete state-ment of all relevant issues.

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