

Committee(s) Property Investment Board – For decision	Date: 12th September 2018
Subject: All Funds – Request for Funds to Appoint External Consultant for an Environmental Strategy	Public
Report of: The City Surveyor (CS.380/18)	For Decision
Report author: Corporate Energy Manager	

Summary

This paper outlines proposed steps to understand, measure and optimise sustainable building performance across the City of London Investment portfolio with specific regard to:

- Understanding cost, compliance, reputational risks and opportunities relating to the investment estate associated with sustainability performance.
- Understanding the Investment portfolio present performance and peer context in respect of sustainable building certification such as BREEAM and SKA.
- Identifying a strategy with actions to deliver commercially sound, environmentally sustainable performance.

Recommendation

Members are asked to:

- Agree to the commissioning of a specialist sustainability consultant to identify a strategy for measuring and optimising environmental performance in a commercial property context at an estimated cost of £55,000.
- Note, as the City Surveyor has no funds available to cover the cost of the work, should Members wish to proceed the City Surveyor will need to make a bid for funding from the Transformation Fund to cover the cost of the work.

Main Report

Background

1. The commercial implications of the sustainability agenda have been growing in the UK commercial property market for some years in terms of both compliance requirements and voluntary reporting. This has been manifested through more stringent environmental legislation such as the EU Energy Performance of Buildings Directive and Minimum Energy Efficiency Standards (MEES), which now represent an embodied element of commercial property management. This represents a step change in legislative impacts in that non-compliance can now affect an organisations ability to trade rather than simply increasing operating costs or administrative compliance. In addition, industry bodies such as the British Property Federation, Better Buildings Partnership and the UK Green Buildings Council are defining best practice and thereby re-defining market expectation in this area in terms of both landlord and occupier groups. Given the context of recent acceleration of energy price increases and the adoption of the City's new Responsible Business Strategy it is a timely opportunity to review the property investment portfolio sustainability policy, having regard to our peer group of other major property funds.
2. With regard to the evolution of the sustainable buildings market and changes in tenant expectation more broadly, it is also a timely opportunity to review the sustainability strategy for the City Corporation's investment portfolio.

Options

3. To provide a commercial view on present performance, risks, opportunities and a recommended strategy we have considered two delivery routes.

- i. **Obtain additional consultancy support (Recommended):** Draw on the expert resources of a sustainability consultant to bring their independent market view

Advantages: Specialist expertise, rapid mobilisation, market knowledge

Disadvantages: Cost of fees

- ii. **Deliver in-house:** While the City has sustainability professionals within the energy team, procurement and built environment, spare capacity of these resources is very limited, as is the current expert knowledge available to deliver this specialist strategy.

Advantages: No additional cost

Disadvantages: Insufficient resource to deliver

4. We recommend this Committee approves Option i - Consultancy support to ensure a rapid mobilisation and draw on wider market experience. An outline scope is given below.

Proposals

5. This paper proposes the commission of a specialist sustainability consultant to identify a strategy for measuring and optimising environmental performance in a commercial property context, specifically:

Phase 1 – Identification and positioning

- Meet and engage with main stakeholders and understand estate profile, existing progress, constraints and develop a strategy.
- Undertake a high-level review of the Corporation's Investment Property Portfolio to establish where material risk and opportunity lies, e.g. occupation / tenancy type / refit / lease renewal.
- Identify tenant expectation and risk transfer relating to the Investment Property portfolio, particularly with respect to Green Lease and Minimum Energy Performance Standards.
- Investigate the potential impact of adopting a higher sustainability standard with regards to rental income and capital invested and the consequent influence on returns. i.e. whether higher standards generate enhanced rents and performance, or whether it dilutes the return on capital investment.
- From this identify a peer group and industry comparator for the City to allow a fair comparison of sustainability performance against policy position and appropriate industry metrics.

Phase 2 – Strategy

- Undertake a market review to include compliance issues such as Minimum Energy Efficiency Standards (MEES), revised planning requirements and tenant expectation and the potential impacts this will have for the City.
- Identify appropriate standards – BREEAM, SKA, LEED, WELL etc with relevant performance levels for the City to consider whether PIB should adopt them as a performance standard (some of these standards already exist within some departments).
- Review the present and future requirements for a Green Lease option or Memorandum of Understanding with Corporation tenants. In particular to understand potential impacts on resources, risk and marketability.
- Identify principal requirement for standardised procedural and technical specifications to support the delivery of these standards, e.g. cooling, lighting, control.
- Provide an indication of any potential implications for capital, revenue, yield, income and officer resource with a simple mobilisation plan.

Output: A paper identifying principal risks and opportunities with an action plan.

Corporate & Strategic Implications

6. This review would support the work currently being undertaken across the City to strengthen our commitment to sustainability. Building on existing strategies designed to minimise the City's environmental impact, such as the Responsible

Procurement Strategy and the most recent Renewable Electricity Policy and Sourcing Strategy. It would also compliment the new Responsible Business Strategy 2018-23: Towards a Sustainable Future and emerging Climate Action Strategy which is being developed by the City of London Corporation on behalf of all businesses in the Square Mile.

Implications

7. This work will identify the City's recommended strategy to sustainable building development across the Investment Property Portfolio. It will identify the impact on rents (if any) and on returns (positive and or negative) of additional sustainability standards. Following an engagement exercise and analysis, a paper will be produced outlining approach and priority actions required. We anticipate the delivery of a draft report within 16 weeks of funding approval and following a mini-tender exercise.
8. Sustainable specifications identified in phase 2 would have the potential to provide:
 - Reduce operating costs (energy, waste water)
 - Improve life cycle costs (maintenance, disposal replacement)
 - Improve working environments (productivity, tenant satisfaction and well being)
 - Reduce asset risk, (resulting from non-compliance with MEES legislation)
9. The sustainability expert would require broad property market experience to provide context, peer positioning and a strategy to allow the City to protect its reputation and commercial interests in relation to sustainability. Estimated costs reflect this level of necessary expertise and are estimated as follows:

Value for money & affordability

10. In developing the strategy, the issues of affordability versus maximising performance and rent, together with value for money will be important in selecting the appropriate standards and should be viewed in the context of achieving of both environmental performance and short and long-term financial metrics. Any strategy needs to be considered in the context of the financial performance metrics which are required to be met on all refurbishment and redevelopment projects across the investment property portfolio. Industry accepted environmental standards should be considered as an alternative, and indeed are currently being implemented on all Investment Property projects in accordance with planning requirements, particularly where the cost implications of implementing any enhanced environmental standards demonstrate that the financial performance of any project would not meet the agreed metrics.

Phase 1. Identification and positioning; - £15k

Phase 2. Strategy: - £40k

Conclusion

11. We propose to review the City's peer position on sustainability in respect of the Investment Property portfolio. The output, if required, will identify an action plan to deliver the practical implementation of an ongoing commercially practicable model for sustainable buildings, which would be implemented on a case by case basis depending on the financial performance metrics for any proposal. This will identify future cost and reputational risks and provide the basis for a mitigation plan, not doing so would potentially expose the City to an unknown risk profile.

Background

A similar paper has recently been submitted to CASC with respect to the operational portfolio and there may be synergies and cost savings in co-commissioning a strategy report should both approaches be endorsed.

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