
Energy Efficiency and Buildings

Summary

- IIGCC believes the EU is showing appropriate concern about energy efficiency in buildings and related carbon emissions, and is generally promoting sound policies in this regard. Sadly, some flagship policies are poorly conceived and only partially implemented.
- In line with academic research, IIGCC believes regulations and standards to be the most cost-effective way to change the behaviours of real estate market participants. This said, the full range of fiscal tools has yet to be explored.
- While acknowledging the need to continually improve standards for new construction and major refurbishments, the IIGCC urges EU policy-makers to think more deeply about improving the performance of *existing* buildings where the bulk of the emissions lie.
- The IIGCC rejects as sub-optimal and inefficient, the notion of funding ‘exemplar smart cities’. Rather, the EU should focus on developing informational networks that facilitate the transfer of best practice to all those who are interested and/or can make use of it. There is no lack of ideas just a failure of widespread implementation.

Introduction

This paper reports the outcomes of a discussion at an investor roundtable convened by the IIGCC on how EU and Member State policy can support increased investment in energy efficiency in buildings. The discussions at the roundtable were partly informed by a background document prepared by the law firm Norton Rose which provided an outline of the regulatory landscape in the EU and its impact on investments in energy efficiency in property.

“Most building owners and users don’t know enough and don’t care enough about energy consumption and inertia is reinforced because first costs are too high and savings are too low.”

World Business Council for Sustainable Development (WBCSD), 2009

The IIGCC is pleased that EU policy-makers increasingly appreciate the significant potential of the built environment for reducing energy consumption and carbon dioxide emissions in today’s Europe, and are prioritising actions in this regard to realise that potential. Following the WBCSD, there is a acute need to (a) help building owners and users care and know more about energy consumption and (b) to make investment in energy efficiency more obviously beneficial to those we depend on to do so.

The following sections critically review the main policy initiatives currently being pursued by the EU and makes relevant observations and recommendations.

Legally binding targets for carbon emissions

The IIGCC believes that not only are such targets welcome but also, for reasons of clarity, focus and accountability, they should be sector specific.

Expanding the control of building regulations

In line with academic research, IIGCC believes that building regulations are cost-effective and influential in changing the behaviours of market participants. However, it urges far more consistency in the level of regulations and the adoption of more stringent enforcement, across the EU. It is widely believed that builders can too easily flaunt existing rules and escape with only a light penalty. However, the absence of clear data on this suggests research is urgently needed.

If the EU is serious about tackling environmental standards in buildings, possibly even amending existing regulations to capture more minor works as well, then enforcement activity needs to be dramatically improved.

Energy Labelling – the Energy Performance of Buildings Directive (EPBD), building regulations and other measures

IIGCC welcomes the improvements being made in the 2010 revision of the 2002 EPBD which will expand its remit across a greater proportion of the built stock, and in a more meaningful way than hitherto. However, it believes that manifold issues with its implementation, if left unaddressed will mean that the EPBD will continue to fail to produce the results expected and desired from it. The application of the current system of Energy Performance Certificates (EPCs) is patchy across the EU, the standards of EPCs issued varies enormously both across and within Member states, and the continuing technical criticism and the highly variable quality of EPCs issued is causing them to be increasingly discredited in the property market. This means they are increasingly being relegated to mere 'licences to trade' rather than playing their part in improving both the energy efficiency and operational standards of buildings.

IIGCC urges that EU policy-makers improve the EPBD further to better capture the actual rather than the potential energy performance of buildings.

Given EPCs are only created as properties are transacted and when built, they will remain only a partial assessment of the existing built stock for some time. The IIGCC urges the EU to consider instigating some kind of building stock 'audit', possibly with government aid and linked to EPC standards improved as described above. Once the state of the European property stock is fully recorded, the EU could require Member States to regularly audit the environmental standards of the existing stock. Not only would this monitor progress but, as suggested in the next sub-section, could also be used for more innovative fiscal approaches in support of energy efficiency.

The EU should be wary of instigating overly simplistic policies based on building quality grades. For example, setting aside the lack of trust in EPCs and the practical difficulties of landlords entering properties to carry out the necessary works, an insistence that all properties should be remediated to or might only be transacted at Grade F level or above, needs to be considered in the light of its potential to cause buildings to be abandoned leading to urban blight or accelerating the 'carbon event' that is redevelopment.

The potential for using market-based mechanisms

The price of carbon remains too low to engender much, if any, behavioural change in the property market. However, IIGCC firmly believes that carbon trading schemes, such as the UK Carbon Reduction Commitment (CRC), have the potential to change this. The example of the CRC offers the EU the chance to learn about how best to implement such schemes elsewhere in Europe. For example, teething problems for the CRC with respect to UK commercial property relate largely to the failure to understand how it operates through the prevailing lease structures- landlords contract with energy suppliers and pass the bills through to tenants but have no direct means to influence tenant behaviour with respect to energy use. Landlord performance is assessed under the CRC on something they are unable to affect directly. This could exacerbate what is already a potentially adversarial relationship between landlords and tenants.

The potential of further fiscal measures

IIGCC feels strongly that there is substantial untapped scope within existing tax regimes to change investor and occupier behaviours towards lower energy use and carbon emission from buildings. Clearly, this potential is largely dependent on having trusted and universal measures of building energy performance upon which such taxes could be based. With this, existing taxes (such as transfer taxes, local property taxes, etc.) could be adjusted using multipliers of greater and less than 1.0, for buildings of different environmental quality. If calibrated correctly, such policies could be made tax neutral.

Smart cities

While acknowledging the potential merit in exhibition projects, IIGCC believes that the EU proposal for exemplar 'smart cities' and any competitive process related to it would be an unnecessary diversion of valuable EU, Member State, Regional and Metropolitan government resources. The current issue is not one of a lack of 'know-how' but one of implementation and take up. There are already many cities authorities and industry experts only too willing to demonstrate their best practices. What is needed is not 'smart cities' but accessible 'smart libraries' and data-bases where those best practices and contact details can be placed, either voluntarily or through academic enquiry, such that others can access and follow up. EU policy-makers must further realise that the ability to materially change the spatial organisation of land uses in mature European cities is very limited, incremental and largely based on transport rather than real estate policy.

Other issues and comments

IIGCC urges the EU and its Member States to convey a long term future consistency in approach to issues such as energy efficiency in building. This will make it clear to real estate market participants that standards and regulations in this crucial area are moving in a set direction. This should lead them to plan and begin to price assets on this basis.

IIGCC believes that the EU and its Member States have a key role to play in educating market participants on why real estate is so crucial to the fight to reduce energy use and mitigate carbon emissions, how they can individually make their contribution, and how such actions align financial and environmental benefit. It is imperative this education is not confined to construction professionals. Rather, it needs to include property investors, occupiers and market agents and brokers.

It goes without saying that governments at all levels need to show leadership in their own responsible occupation and ownership of buildings. They should also be monitored and held to account in this regard.

The IIGCC believes that the current proliferation of environmental metrics, labels and standards is increasingly perplexing for market participants and risks engendering inaction and prevarication as they struggle to understand what to do for the best. While supporting the general principle of information transparency, the IIGCC urges the EU to work hard with organisations producing such measures to accelerate standardisation, consistency and comprehensiveness.

The IIGCC believes that the agency and brokerage community is a key opinion former in the marketplace and has yet to show much responsibility in promoting the virtues and financial potential of adopting energy efficiency in buildings. The EU and Member State governments should urge codes of behaviour for this important group obliging them to promote the benefits of energy efficient buildings and the merits of 'green lease' provisions.

The IIGCC notes and supports EU policies on ESCOs and National Energy Efficiency Funds (NEEFs). However, such initiatives are unlikely to be of direct relevance to capital owners and property investment managers of the scale and focus represented in the IIGCC membership. As such, we wish the EU success in this regard but have no detailed comments to provide other than to say that such measures will only affect behaviours across a modest proportion of the real estate market, and are insufficient to meet EU aims.

The IIGCC is primarily an asset owner and manager-based organisation. For long periods when their buildings are occupied, its members have little influence over the main energy users in buildings, the occupiers. It is, therefore, imperative that the EU finds ways to change the behaviour of building users. This may require similar approaches to those mentioned above (e.g. regular audits of building performance influencing local property taxes, etc.), there may be specific measures affecting tenancies that could be adopted, or there may be general measures to make occupiers 'care more' about energy efficiency (e.g. by simply raising the price of carbon sufficiently).

Finally, it is important that policy-makers at all levels of government understand that development is but one modest aspect of real estate. Properties go through an extended life cycle of development, usage, periodic rounds of work and, finally, demolition. Each stage involves different parties with different interests and motivations. This means that policies to drive responsible behaviours may well vary depending on what stage a building is at and which parties are involved. As such, to achieve its aims, there is need for the EU to develop a coherent set of policies to drive mutually reinforcing behaviours across all parties over the whole life cycle of a building.

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About IIGCC

The Institutional Investors Group on Climate Change (IIGCC) is a forum for collaboration on climate change for European investors. IIGCC's ambition is to provide European investors with a voice on climate change and engage with companies, government and investors on addressing long-term risks and opportunities associated with climate change. The group currently has over 60 members, including many of the largest pension funds and asset managers in Europe, representing assets of over €5trillion.

In detail, the IIGCC's objectives are:

- To encourage public policy solutions that ensure an orderly and efficient move to a low carbon economy and adaptation measures which are consistent with long-term investment objectives.
- To encourage a pro-active approach on climate change amongst asset owners and asset managers in order to preserve and enhance long-term investment values.

To improve company disclosure and performance on climate change.

IIGCC Membership, September 2010

Alfred Berg	HSBC Investments
Amundi	Hudson Clean Energy
APG Asset Management	Impax Asset Management
ATP	Insight Investment
Aviva Investors	Invicta Capital
Baptist Union of Great Britain	Joseph Rowntree Charitable Trust
BBC Pension Trust	Kent County Council Pension Fund
Bedfordshire Pension Fund	London Borough of Hounslow Pension Fund
BlackRock	London Borough of Islington Pension Fund
BMS World Mission	London Borough of Newham Pension Fund
BNP Paribas Investment Partners	London Pensions Fund Authority
BT Pension Scheme	Merseyside Pension Fund
CB Richard Ellis Investors	Northern Trust
CCLA Investment Management	Osmosis Investment Management
Central Finance Board of the Methodist Church	PGGM Investments
Church Commissioners for England	PKA
Climate Change Capital	PRUIM
Co-operative Asset Management	Robeco
Corporation of London Pension Fund	Schroders
Earth Capital Partners	Second Swedish National Pension Fund
Environment Agency Pension Fund	South Yorkshire Pensions Authority
Environmental Technologies Fund	The Church in Wales
Ethos Foundation	The Church of England Pensions Board
F&C Management Ltd	The Roman Catholic Diocese of Plymouth
First Swedish National Pension Fund	The Roman Catholic Diocese of Portsmouth
Fourth Swedish National Pension Fund	The Roman Catholic Diocese of Salford
Generation Investment Management LLP	Third Swedish National Pension Fund
Good Energies	United Reformed Church
Greater Manchester Pension Fund	Universities Superannuation Scheme
Grosvenor Fund Management	West Midlands Metropolitan Authorities Pension Fund
Henderson Global Investors	West Yorkshire Pension Fund
Hermes	William Leech Charitable Trust
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