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## The Non-Domestic Private Rented Sector Minimum Energy Efficiency Standards – The Future Trajectory to 2030

### Response of the Commercial Real Estate Finance Council (CREFC) Europe

The Commercial Real Estate Finance Council (**CREFC**) Europe is a trade association promoting a diversified, sustainable and successful commercial real estate (**CRE**) finance market in Europe that can support the real economy without threatening financial stability. Our membership includes a range of different bank and non-bank lenders, intermediaries and advisory businesses, and real estate firms that use debt to finance their activities.

Energy efficiency and sustainability issues have become increasingly mainstream issues for the CRE lending community in recent years, both in the UK and more generally across our membership. In part, this is because of a growing focus specifically on climate change issues, but also more broadly on ESG considerations; but an additional and very important driver was the UK's introduction of minimum energy efficiency standards (**MEES**) for non-domestic property, which made the subject impossible for lenders to ignore in due diligence and risk management. We welcome the Government's consultation on the trajectory for non-domestic PRS MEES and are pleased to provide our input.

It is important to emphasise that, despite lenders' increasing interest in the sustainability characteristics of the real estate collateral for their loans, it is the borrower (i.e. the real estate investor) that remains primarily responsible for ensuring that its assets are compliant with MEES (and more generally resilient to sustainability-related risks). In essence, lenders must satisfy themselves that their borrowers' buildings are MEES compliant and that they have a suitable strategy to ensure compliance with changing requirements in the future; it is not the role of lenders to respond directly to MEES by transforming buildings themselves.

As a result, our approach in responding to this consultation has mainly involved engaging with the work of other organisations whose draft responses we have seen, notably the British Property Federation (**BPF**) which, in its role as representative of the UK real estate sector, is best placed to comment on the Government's proposals, and the Better Buildings Partnership (**BBP**), with which we have partnered in recent years in looking at sustainability from the lender perspective.

#### Headline response

We agree with the responses of the BPF and the BBP, both in supporting the setting of a clear and ambitious trajectory for MEES for the next decade, and in noting a number of relatively fundamental issues that seem likely to impede the effectiveness of MEES in delivering the contribution of the UK's commercial real estate to the transition to a low carbon economy. Concerns we would emphasise include the following.

- The fact that EPC ratings are widely perceived to be unreliable and inconsistent, and in any event a poor guide to the in-use/operational energy performance of buildings, which is what really matters in terms of tackling climate change. This is linked to the perennial problem of mismatches as to where, among building owners and building occupiers, the risks, benefits, costs and compliance burdens fall, particularly given the highly heterogeneous nature of commercial buildings and the variety of leasing and occupational arrangements that exist.

- The challenges that many buildings and building owners may face in funding the work required to upgrade buildings to the required level. One lender in our membership which should be well-positioned to deal with MEES (it has a relatively small number of relatively large loans secured on high quality, well located and often new buildings) notes a surprisingly large proportion of the properties against which it has lent would require work to achieve a B rating, or only marginally achieve it. The equity and debt that the industry as a whole will require to upgrade buildings by 2030 may be more than is currently expected, and may not be available for structurally problematic parts of the market (such as poorer quality retail assets), or in the event of a significant market downturn in the intervening years. Given that it is often impossible to make necessary upgrades to existing buildings save during occasional periods of vacancy, the time for interventions between now and 2030 may in practice be very limited.
- It is not clear, from a broader policy perspective, what is intended for buildings that MEES render unlettable because required upgrades are unfundable or economically unjustifiable.

## Responses to specific questions

**Question 1:** We have nothing to add to the responses of the BPF and BBP, which we support.

**Question 2:** As noted above (and by the BBP in its response), we believe that the introduction of MEES played a significant role in putting energy efficiency and sustainability considerations firmly onto the radar of commercial real estate lenders. Beyond that, we note and agree with the comments made by the BPF and BBP in their submissions.

**Question 3:** We have nothing to add to the responses of the BPF and BBP, which we support, subject to reiterating that the importance of signalling the urgency of action with an ambitious trajectory should be qualified by recognition that deliverability may be challenging for parts of the market.

**Question 4:** We have nothing to add to the responses of the BPF and BBP, which we support.

**Question 5:** We agree with the points made by the BPF and BBP in their submissions. We are especially concerned (a) that the strong regulatory focus on EPC ratings risks distracting market participants from more practically important interventions (relating to the in use / operational energy profile of buildings), and (b) that the equity and debt capital required to achieve the proposed MEES trajectory may not be available on economic terms from the market.

**Question 6:** We have nothing to add to the responses of the BPF and BBP, which we support.

**Question 7:** We have nothing to add to the responses of the BPF and BBP, which we support.

**Question 8:** We have nothing to add to the responses of the BPF and BBP, which we support, with the exception of the BPF's suggestion that the Government consider making grants or low interest loans available to incentivise building upgrades. While financial support from Government may well be required in this policy area, it needs to be considered carefully so as to avoid cutting across efforts by the lending industry to support sustainability-related building improvements. Indicative of the level of market interest in this area is our very recent launch of a working group on 'green' commercial property lending with strong support from a wide range of lending firms in our membership.

**Question 9:** We have nothing to add to the responses of the BPF and BBP, which we support.

**Question 10:** We have nothing to add to the responses of the BPF and BBP, which we support.

**Question 11:** We have nothing to add to the responses of the BPF and BBP, which we support.

**Question 12:** We have nothing to add to the responses of the BPF and BBP, which we support.

**Question 13:** We have nothing to add to the responses of the BPF and BBP, which we support.

**Question 14:** We have nothing to add to the responses of the BPF and BBP, which we support.

**Question 15:** We have nothing to add to the responses of the BPF and BBP, which we support.

**Question 16:** We have nothing to add to the responses of the BPF and BBP, which we support.

**Question 17:** We have nothing to add to the responses of the BPF and BBP, which we support.

If you have any queries in relation to this submission, please contact Peter Cosmetatos, chief executive of CREFC Europe, on 020 3651 5696 or [pcosmetatos@crefceurope.org](mailto:pcosmetatos@crefceurope.org).