

# Overcoming Split Incentives in Office Buildings: The Utility Role

## Leased Offices: A Key Market Segment

Because **90%** of California's commercial office space is leased, rather than directly owned, it is essential to address the barriers associated with greening *leased* space.

### KEY CHALLENGES TO GREENING IN LEASED BUILDINGS

- High First Cost for Many Retrofits
- Complex, Specific Arrangements Needed for Each Lease
- No Single Green Standard For All Building Types, Areas
- **Split Incentives** for Building Owners and Tenants

### The Split Incentive Barrier

TYPES OF EFFICIENCY IMPROVEMENTS	OWNER PERSPECTIVE	TENANT PERSPECTIVE
Core and Shell Retrofits	Owner bears cost for construction and major building retrofits, but does not benefit from all utility savings	Tenant wants lower utility costs, but has limited timeframe and limited knowledge of building engineering issues
Tenant Space Retrofits	Owner does not pay utility costs, but may fund or approve TI	Tenant wants lower utilities, but function, aesthetics, and first cost are more important
Building Operations Optimization	Owner must meet diverse tenant needs in building operations and maintenance	Tenant wants comfort, ease of use, and lower costs

## The Green Leases Toolkit

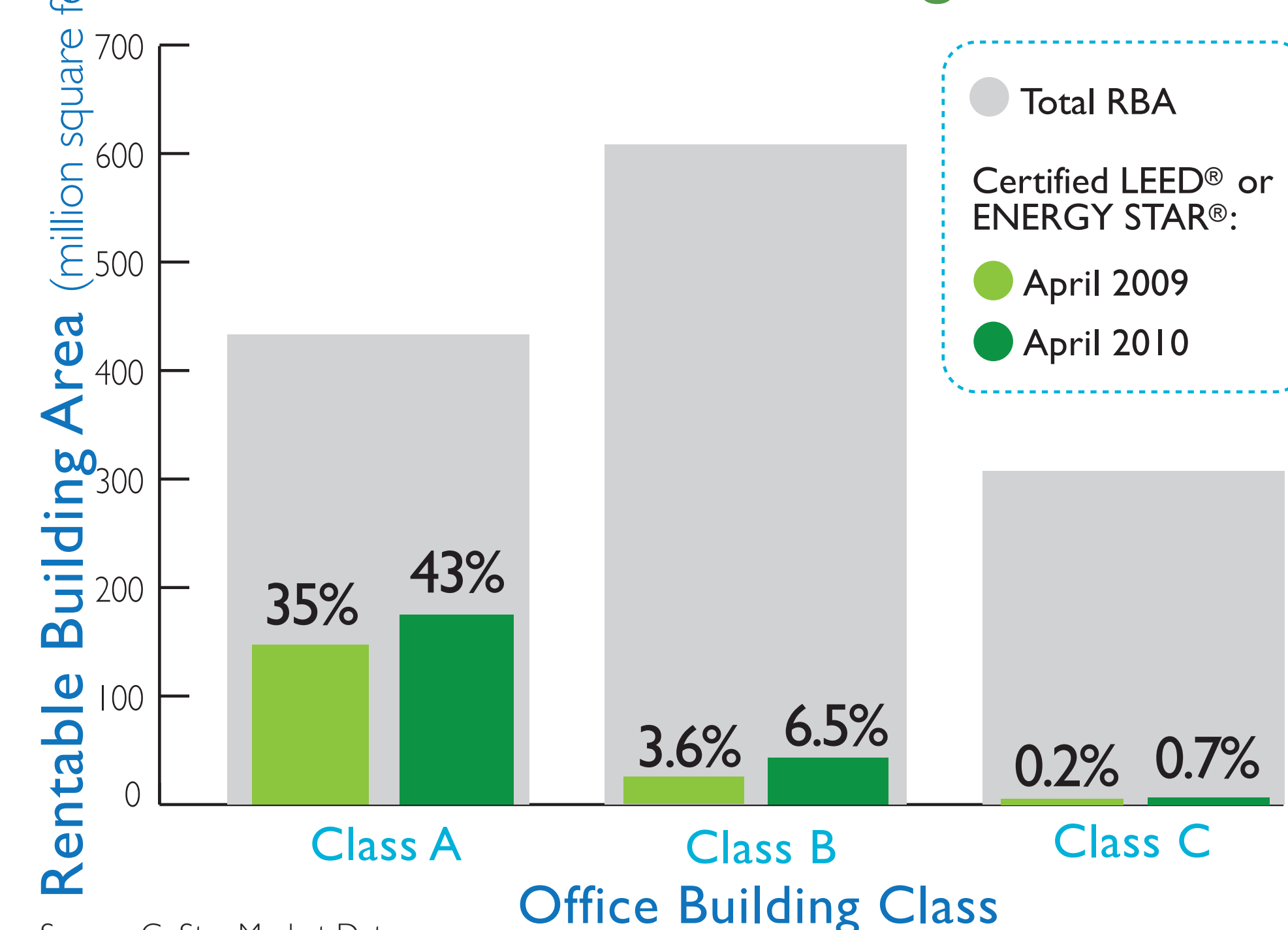
Developed by Navigant Consulting and the California Sustainability Alliance in 2008, the Green Leases Toolkit identifies how sustainability can be incorporated into the entire leasing process, from both the tenant and landlord perspectives. The Toolkit provides sample language, checklists, scorecards, other resources to help tenants and landlords adopt green leasing. To be effective, green leasing concepts must be integrated into the leasing process from the very beginning, not just during lease negotiations.

Founded in 2006, The California Sustainability Alliance is funded by California utility customers and administered by Southern California Gas Co. (The Gas Company) under the auspices of the California Public Utilities Commission, through a contract awarded to Navigant Consulting.



## Why focus on office buildings?

### California's Green Building Barometer

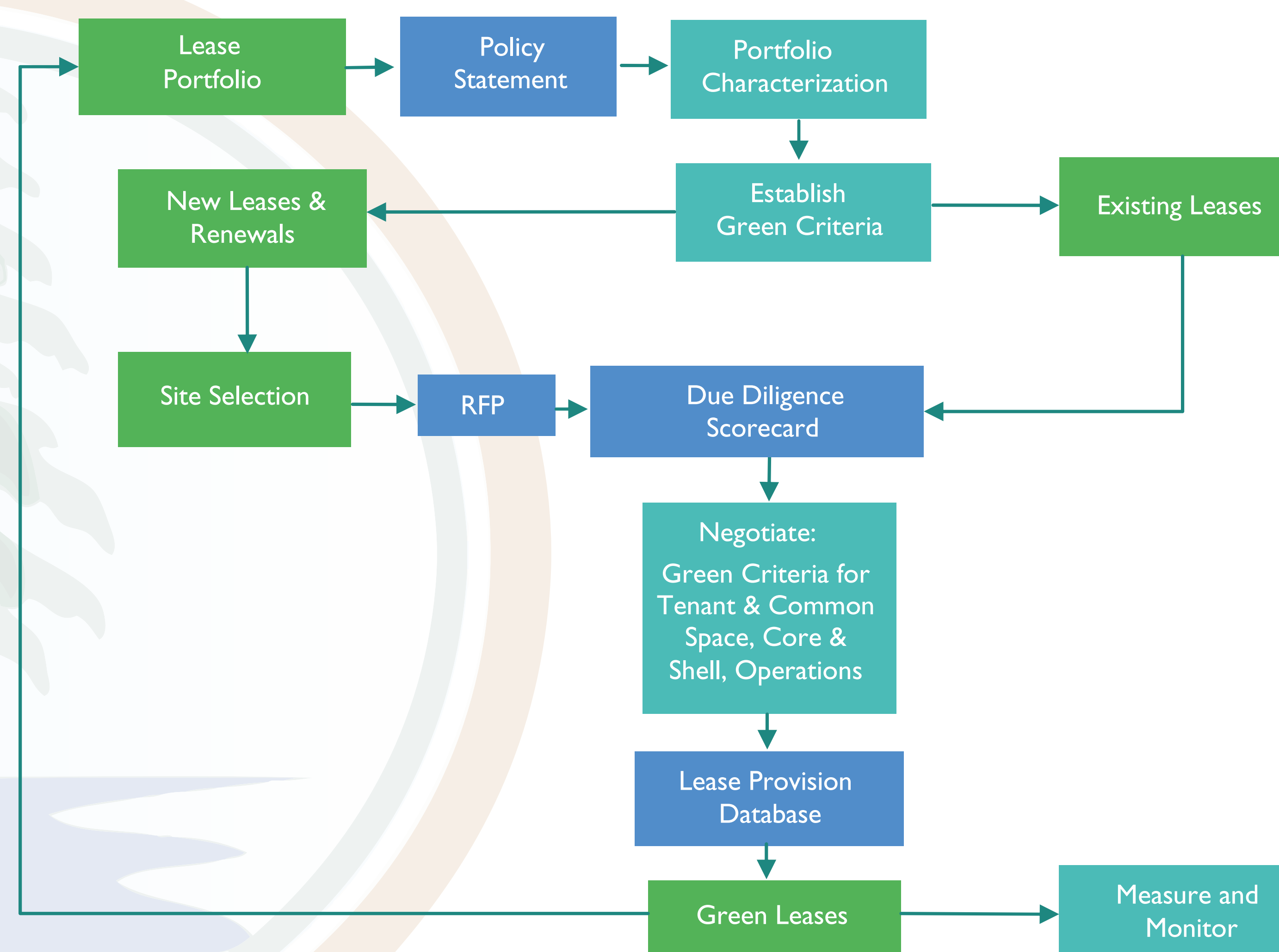


- Commercial office buildings consume over 180 MTherms of natural gas and 16 TWh of electricity each year in California, corresponding to **14%** of natural gas consumption and **24%** of electricity consumption in the commercial sector, statewide. (CEUS, 2006)
- Today, 19% of office space in California has some form of green certification (LEED® or ENERGY STAR®). Over four fifths of that "green" space is in Class A office buildings, which comprise only one third of total office building square footage. (CoStar, October 2010)

## Potential Programs Utilizing the Green Leases Toolkit

- Utility-facilitated education and outreach workshops for tenants and owners, leveraging existing utility contacts and marketing initiatives
- Technical assistance for due diligence
- Incentives and/or recognition for owners and tenants who commit to adhering to the green leasing process
- A platform for owners and tenants to share information about their sustainability needs or offerings, and connect with potential green lease opportunities

### The Green Leasing Process



## Potential Programs Beyond the Green Leases Toolkit

### REBATES

- Rebates to both owners and tenants
- Incentives for submetering
- Incentives to offset legal/time costs associated with changing lease terms
- Enhanced incentives for whole building and/or whole portfolio retrofits to encourage adoption of sustainability as standard practice

### FINANCING

- On-bill financing programs to fund retrofits; payment of the monthly surcharge can be negotiated between tenants and owners
- Separate financial assistance programs for building owners and tenants to address the unique perspective and needs of each participant in the leasing process

### MARKETING, EDUCATION, AND OUTREACH

- Technology education for building owners and tenants, including information on how adoption of green technologies can be incorporated into lease language and can benefit both owners and tenants
- Utility-facilitated dialogue and data about the costs and benefits of green building retrofits, to identify cost-effective opportunities
- Program outreach targeting the full range of building owners and tenants, from Class A to Class C
- Facilitation of ENERGY STAR® rating for building owners; buildings that score well can incorporate their score into marketing materials, while buildings that score poorly can use the benchmark as a starting point for improving sustainability

**While financial incentives are needed, marketing, education, and outreach are more essential to overcoming split incentives in leased buildings.**