PUBLICATION

Green Building: Good for the Planet and Your Pocket

April 22, 2009

Summary: *The green building trend is positioned to emerge from the current economic downturn stronger than ever. The United States Green Building Council is piloting two new retail-specific LEED certification programs in 2009, and retailers and landlords alike are recognizing that not only should they be held accountable for the effects of their buildings on the environment, but that such accountability can ultimately prove beneficial for their bottom lines.*

There is no doubt that these are difficult times for the commercial real estate industry, in general, and the retail industry, specifically. The current economic slowdown, however, may ultimately prove beneficial for both as an opportunity to re-evaluate current business practices, to change, and to grow. Evaluation, change and sustainable growth are cornerstones of the green building movement, which has persisted in the midst of the current downturn. In fact, in 2009, the United States Green Building Council (USGBC) is launching two new LEED (Leadership in Energy and Environmental Design) rating systems which are retail-specific. As will be detailed below, these new certifications will be highly sought after, even in the midst of the current financial crisis. Why? Because not only do tenants and landlords realize that it is in their best interests to green the planet, they also realize that, by doing so, they will be greening their pockets as well.

In 2008, participation in the two most popular sustainable building programs—USGBC LEED certification and the Energy Star label for energy efficiency—increased dramatically. Two thousand buildings received the Energy Star label in the first eleven months of 2008, which is a quarter of the total labelings in Energy Star's ten year history, and certified LEED projects more than doubled in 2008. As of April 2008, more than 867 million square feet of space were LEED certified, internationally. So what is LEED certification and why is it so sought after?

LEED is a voluntary certification that is based upon site selection, indoor air quality, water and energy efficiency, and materials and resources used. To achieve a certain level of certification (such as LEED Platinum, Silver or Gold), buildings must comply with certain prerequisites and earn points, also known as credits. The credits are then compiled into rating systems, which are based upon a range of building types. Until recently, however, the LEED rating system failed to address several characteristics unique to retail buildings. For example, while office buildings have long-term employees, consistent water usage and office specific lighting, energy usage in retail buildings is often sporadic, as customer traffic fluctuates with the shopping seasons. Moreover, retail spaces such as restaurants use high-energy equipment like refrigeration systems, commercial dishwashers and washing machines, and kitchen equipment. The prior LEED rating system failed to take these retail-specific nuances into account.

Due to these and other retail-specific concerns, the USGBC and over eighty pilot project teams are collaborating to create two new rating systems in 2009: LEED for Retail-New Construction (NC) and LEED for Retail-Commercial Interiors (CI). LEED for Retail-NC encompasses new and newly renovated standalone buildings, whereas LEED for Retail-CI enables tenants of shopping centers or other adjoined buildings to certify a revamping or build-out of their retail space. The pilot programs will include quick-service restaurants, large-format retailers, stand alone stores, and banks.

Similar to the other LEED rating systems, LEED for Retail will be based upon a point system, ranging from the minimal twenty-six points (LEED Certified) to the maximum seventy points (LEED Platinum). In addition to the standard LEED certification prerequisites, parking and transportation are crucial elements of LEED for Retail, which gives credits for retailers that provide preferred parking for employees and fuel-efficient vehicles, and also gives credits to those retailers that offer incentives to employees who ride public transportation or who participate in carpool arrangements for work-related driving.

LEED certification is by no means easy, as standards are stringent and the paperwork is extensive. LEED certification is by no means cheap either, as registration fees, application fees, and fees paid to LEED consultants add up quickly. Nevertheless, retailers and shopping center owners continue to seek LEED certification as a result of their recognition of corporate environmental responsibility, the availability of a vast array of financial benefits and incentives, and legislation mandating change.

Corporate environmental responsibility is now considered mainstream. Such responsibility is demanded by both consumers and retailers, and for good reason. Commercial buildings consume massive amounts of energy, the production of which creates greenhouse gases, which are the primary contributors to global warming. In North America, energy consumption by commercial buildings represents between ten to twenty percent of all energy consumption. This energy includes natural gas and electricity for heating, the running of electrical systems, and cooling. One need not adhere to the "Inconvenient Truth," however, to have a reason to reduce energy consumption, as there are a plethora of important local reasons to do so, including poor air quality conditions, excess storm water drainoff and water shortages.

Retailers are finding that such accountability, including green building practices, is also proving beneficial for their bottom lines. Research shows that green buildings have higher occupancy and rental rates, lower operating expenses and higher sales prices than their non-green counterparts. Specifically, USBGC claims that feasible financial benefits of making buildings greener include:

- 30 to 50 percent energy savings;
- 35 percent savings on carbon emissions;
- 40 percent water savings;
- 30 percent savings on solid waste;
- 6.6 percent average improved return on the investment;
- 8 to 9 percent decrease in total operating costs;
- 3 percent higher rents; and
- 3 percent higher occupancy costs.

While the up-front costs for building green are typically two percent higher than non-green buildings, this cost is recouped between twelve and twenty-four months after construction, on average.

Moreover, state and federal legislation has been passed which provides tax incentives, rebates and other financial assistance to promote further growth in the green building industry. The leading federal incentive is the Energy Efficient Commercial Building Tax Deduction (26 U.S. Code Sec. 179D) for energy efficiency in retail stores, shopping centers and other commercial buildings. Section 179D (recently extended through 2013 by Section 303 of the Energy Improvement and Extension Act) allows a commercial building owner to deduct part or all of the cost of certain "energy efficient commercial building property." The amount of the deduction is typically equal to the cost of qualifying property placed in service during a taxable year, subject to a cap of $1.80 per square foot. This deduction is generally available to owners who install (1) interior lighting; (2) building envelope or (3) heating, cooling, ventilation or hot water systems that reduce the building's total energy and power cost by fifty percent or more in comparison to a building meeting minimum requirements set by Standard 90.1-2001 of the American Society of Heating, Refrigerating, and Air Conditioning Engineers and the Illuminating Engineering Society of North America.

The green movement has also been boosted significantly by mandated sustainable building legislation, which is rapidly spreading not only throughout the United States, but throughout the world. Twenty-two states and more than fifty municipal governments have passed legislation mandating LEED-certified public buildings when public funds are used to build them. Some cities and states are also incorporating green building requirements into building codes affecting both private and public development projects. For example, in 2006, Babylon, New York adopted a comprehensive green building code for commercial buildings tied directly to LEED certification. According to Babylon officials, the new building code could reduce greenhouse gases from the city by 1.37 million tons. Under the new code, Babylon will not issue a building permit unless the permit application includes a completed LEED checklist or other comparable reporting system showing minimum compliance with LEED requirements. The Arches at Deer Park (the first large-scale retail project in Babylon faced with the mandated LEED certification) will span 800,000 square feet, and will combine big-box stores, outlet stores, restaurants and a multiplex theater.

In conclusion, it is likely that green building is positioned to emerge from the current economic recession as a more influential force than before. A recent survey found that seventy percent of corporate executives identified sustainability as a "critical business issue," up more than twenty percent from the previous year. These executives realize that by establishing and meeting sustainability goals, they can improve the image of their companies and save money at the same time. In short, green building and sustainable practices in general will soon become the standard rather than the exception. As one real estate consultant recently noted, "if you're not building green, your buildings are already obsolete."