

Retrofitting multi-tenant buildings for sustainability

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While construction starts for new office buildings are obviously lagging in this economic environment, there has been and will continue to be increased interest by property owners in retrofitting existing buildings.

The desire to retrofit an existing building can be motivated by several factors. For some, it may be desirable to improve the condition of a building to meet the demands of tenants looking for higher quality space and not finding it given the dearth of new construction in certain markets. For others, it may be the desire to increase energy and other efficiencies to reduce operational expenses, perhaps taking advantage of available incentives or tax credits.

And for others, it may be the desire to execute their business plan of owning an asset or portfolio of assets with third-party Green building certification, or alternatively, to cater to tenants who seek to locate in a building with a third-party Green building certification as a result of their own sustainability commitments or objectives.

Regardless of an owner?s motivations for retrofitting an existing multitenant building, there are legal issues that merit attention in planning and executing the retrofit strategy.

To certify or not to certify?

Before commencing a retrofit project, the owner should decide whether or not it is necessary or appropriate to seek third-party certification for the building under the U.S. Green Building Council?s LEED® Green Building Rating System or some other program.

In addition to evaluating the perceived benefits of certification and the costs and risks of pursuing it, that decision will include determining whether or not there any local or other regulatory requirements that require pursuit of certification.

For example, under San Francisco?s green building ordinance that became effective in November 2008, an office building renovation that includes 25,000sf or more can trigger a requirement to obtain LEED certification. With the increased proliferation of these local mandatory Green building ordinances around the

country, including jurisdictions in Florida with such ordinances under consideration, it is important to stay abreast of such regulatory requirements.

Even in the absence of such a regulatory requirement, owners contemplating investing in a retrofit should consider whether their potential tenants might require the building to be certified. For example, some sizable financial institutions and other corporate tenants are adopting corporate mandates to locate only in LEED certified space or space with other environmental attributes or designations. Similarly, some government tenants are required by law to locate in LEED or other certified space.

For example, pursuant to legislation enacted in 2008, no Florida state agency can enter into lease agreements for office space that does not meet Energy Star building standards except when determined by the appropriate state agency head that no other viable or cost-effective alternative exists. Therefore, legal requirements for both owners and tenants can impact the owner's certification decision or obligation.

Pursuit of incentives?

The building owner should also determine whether there are current or pending incentives that can and will be pursued on account of the building retrofit project to be aware of any prerequisites or requirements for obtaining the incentives. An owner's failure to take certain actions could compromise the ability to obtain the incentives.

For example, in Oregon, the state has offered a tax credit for Green building. However, one of the prerequisites to be eligible for the incentives is that the owner must apply for a preliminary certificate prior to commencement of construction and within 30 days of receiving the LEED registration number. Similarly, in Maryland, an owner needs to apply for an Initial Credit Certificate under that state's tax credit program prior to commencing construction of the building rehabilitation project.

Because the regulatory landscape is changing rapidly in the realm of sustainability, incentives and deployment of stimulus funds at the federal, state and local levels, owners should fully investigate the requirements for any incentives or funds they intend to pursue to better ensure compliance with any applicable requirements. It would be unfortunate and potentially damaging to the pro forma to miss an incentive opportunity for failure to comply with the legal requirements for the award.

Leases

Since many multitenant office buildings that are evaluated for retrofit will have existing tenants, an owner should undertake a comprehensive audit of the building leases to determine what barriers might exist to executing the retrofit project.

While I could write an entire lengthy article on the topic of leasing Green buildings, some of the salient concerns will include the ability of the owner to implement energy saving and other operational measures and requirements of tenants to accept or cooperate with same (e.g., Can landlord submeter? Can landlord provide power via an alternative energy system? Can landlord require daytime janitorial in the tenant space to reduce energy use at night? Can landlord access the space sufficiently for measurement and verification?).

Mining the leases and rules and regulations prior to announcing or commencing a retrofit project could afford an owner with an opportunity to revise leases as the opportunity arises with tenants and also understand what leverage tenants have to impede implementation of the project.

Marketing

The same caution I give to developers of new multitenant buildings applies to owners who are retrofitting a building: don't promise (explicitly or implicitly) what you cannot assure delivery of in terms of certification or performance unless you are prepared to accept the consequences if you do not deliver.

When preparing press releases, Web sites, marketing literature or even when corresponding with existing tenants when seeking tenant cooperation for the retrofit project, use sufficient disclaimers regarding owner's objectives for Green building certification or building performance. Retrofit projects aimed at creating a more sustainable building and other sustainability commitments by an owner can result in enthusiastic marketing or leasing agents who need to understand the risk to the owner if inducements or representations are made and then the certification is not obtained or the building does not perform as expected.

In conclusion, while building retrofit is not a new concept, there are unique risks and issues emerging as the retrofit process intersects with new regulatory requirements and third-party Green building certification systems. Owners need to be mindful of these issues to manage their risk while maximizing opportunity.

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