

---

# Environmental upgrade agreements — Implications for councils and commercial building owners and tenants

*Martin Watts HENRY DAVIS YORK*

The State and Federal governments have recently begun a campaign to improve the energy efficiency of commercial buildings in Australia. The Federal Government led the way in July 2010 with the implementation of the Building Energy Efficiency Disclosure Act 2010 (Cth), which imposes disclosure obligations on particular commercial building owners to advertise the energy efficiency rating of their building.

The outgoing NSW Labor Government recently made their own contribution to the movement towards creating more sustainable office space. The Local Government Amendment (Environmental Upgrade Agreements) Act 2010 (NSW) (the Act) passed through NSW Parliament on 24 November 2010 and commenced on 18 February 2011.

The provisions of the Act are designed to facilitate building owners entering into more long term borrowing arrangements with financiers. This will open up the possibility of building owners implementing a range of more significant and longer term projects, resulting in greater improvements to the energy efficiency of commercial buildings.

This regime is fundamentally based upon the 1200 Buildings scheme adopted by the City of Melbourne, which has set the target of being carbon neutral by 2020. The 1200 Buildings scheme also seeks to improve access to funding for commercial building owners who are seeking to retrofit their buildings in order to improve their energy or water efficiency.

The legislation in NSW appears to have used the 1200 Buildings scheme as a prototype for the implementation of their new concept of environmental upgrade agreements (EUAs). The Act inserts a new Pt 2A into the Local Government Act 1993 to promote the funding of projects for the improvement of energy efficiency in commercial buildings and multi-residential strata complexes in NSW.

## Environmental upgrade agreements

Pursuant to s 54D, the Act will allow local councils to enter into EUAs, on a voluntary basis. These will be tripartite agreements between:

- (a) the building owner;
- (b) the financier; and
- (c) the relevant local council.

While any council can take advantage of the scheme, it is expected that EUAs will predominantly be used by council's with a high ratio of large commercial buildings, such as the City of Sydney, North Sydney, Willoughby City, Parramatta, Newcastle and Wollongong Councils.

An EUA will provide for the undertaking of particular "environmental upgrade works". These are defined under s 54E as works for the improvement of the energy, water or environmental efficiency or sustainability of the building.

An EUA can be used in respect of existing buildings for which an occupation certificate has been issued and which are non-residential or a multi-residential strata scheme comprising more than 20 lots, in accordance with s 54F of the Act.

The amount to be borrowed by the building owner to undertake the environmental upgrade works must be set out in the EUA, as well as the repayment arrangements. Pursuant to s 54I of the Act, the council is entitled to levy a charge on the land as security for the repayment of the loan to the finance provider. This charge is referred to as an "environmental upgrade charge".

## Environmental upgrade charges

The environmental upgrade charge is the main incentive under the Act that is intended to encourage banks and other lenders to enter into more long term borrowing arrangements as it provides further security for their loan facilities. Section 54G of the Act prescribes that an EUA must specify:

- (a) the amount of the charge;
- (b) the date/s on which the charges are to be levied by council;
- (c) any adjustments that can be made in the case of late payments;

- (d) the manner in which money paid to council in respect of the charge is to be paid by council to the lender; and
- (e) any service or late payment fees that council will deduct from money paid with respect to the charge.

Under s 54L, environmental upgrade charges are payable within 28 days of notice being served by council on the person liable to pay the charge under the EUA. Charges levied on strata buildings are payable by the owners corporation for the strata scheme, pursuant to s 54K of the Act.

Critically, the Act provides that council is not liable, pursuant to s 54M(2), for the failure of any person to pay the environmental upgrade charge. As such, the council is not liable to pay the outstanding amounts to the lender. However, the council is required to use their “best endeavours” to recover the charge.

This will provide substantial protection to the councils and will give them a greater incentive to enter into these agreements. It is likely that for councils to use their “best endeavours”, they will be required to utilise their enforcement powers under Ch 17 of the Local Government Act.

## Other relevant considerations

The Act also contains specific provisions in relation to lease agreements. One of the difficulties with implementing energy efficiency programs in large commercial buildings is that lessors are often reluctant to outlay expenditure on capital projects of this nature, when it is the lessees who will predominantly reap the benefits through lower outgoings.

The Act addresses this issue with the implementation of s 54N of the Act, by allowing for lease agreements to incorporate terms requiring a lessee to pay a contribu-

tion toward the payment of an environmental upgrade charge. However, the amount recoverable by the lessor is limited to a reasonable estimate of the lessee’s cost savings as a result of the works being undertaken. This provision of the Act will apply despite the operation of s 23 of the Retail Leases Act 1994 and s 40 of the Residential Tenancies Act 2010.

Leases that were entered into before the commencement of the Act that contain a term requiring the lessee to pay the lessor for any charges levied by the council are taken to require the lessee to pay the lessor a contribution towards an environmental upgrade charge.

The council cannot force a building owner to enter into an EUA as a condition of development consent, or under any order issued pursuant to the Environmental Planning and Assessment Act 1979, further to the provisions of s 54O of the Act. However, the Act contemplates that an EUA could form part of a voluntary planning agreement.

The NSW Government has claimed that the property sector, the major banks and the local councils will support the concept of EUAs. While the Act has sought to address the shortcomings experienced with the 1200 Buildings scheme, it remains to be seen over the coming months whether building owners, financiers and the council’s will take advantage of EUAs to implement long term sustainable energy projects.



**Martin Watts,**  
*Lawyer,*  
*Henry Davis York,*  
*Email: martin\_watts@hdy.com.au.*