

This article first appeared in a slightly different form in *Estates Gazette*, 5 December 2009

A NEW-LOOK CARBON REDUCTION COMMITMENT – KEY CHANGES FOR THE PROPERTY SECTOR

By Michael Hutchinson and Darren Berman

The Government recently announced major changes to the CRC. The scheme - now known as the CRC Energy Efficiency Scheme - is key to the Government's targets for reducing greenhouse gas emissions. UK buildings comprise just under 50% of our carbon emissions, so legislation to incentivise emissions reductions in the UK building stock was at some point, inevitable. The implications for occupiers and landowners are many and various. The scheme is administratively complex, with potentially hefty penalties for breaches, "naming and shaming" and even potential director liability.

Whilst the Government's proposed changes deliver some much-needed clarity, confusion over Landlord and Tenant issues, in particular, remain.

Basics of scheme

The CRC is a mandatory carbon trading scheme under which organisations broadly with electricity bills of over £500,000 in 2008 will have to buy carbon credits (or allowances) equivalent to their energy use. Money raised by sale of allowances is recycled back to participants via a cash sum (the "recycling payment") based on a number of metrics at the end of each emissions year, including action taken before the scheme comes into force in April 2010 and absolute emissions reductions.

Key changes

The following is a summary of the headline changes proposed by the Government.

Cash flow

There will now be no requirement to buy allowances in respect of the first year of the CRC (April 2010 to March 2011). Previously, the Government had proposed that at the first sale in 2011, participants would have to buy allowances both retrospectively for 2010/2011 and in advance for 2011/2012.

No option to transfer responsibility for emissions

As a rule, where the Landlord is responsible for the energy supply, it (or its parent organisation) will be responsible for those emissions. The Government had floated the idea of allowing the Landlord and Tenant to agree that the Tenant would take responsibility for compliance with the scheme in certain circumstances. This will, for the time being, not be allowed.

Obligation to cooperate

In order to encourage Tenants to work with Landlords the Government is including an additional provision requiring the Tenant to cooperate with the Landlord for the purpose of complying with the CRC.



Michael Hutchinson (pictured) is a partner and head of the Environment Group at Mayer Brown International LLP.

Darren Berman is Director of Energy and Sustainability at CB Richard Ellis Limited.

A NEW-LOOK CARBON REDUCTION COMMITMENT – KEY CHANGES FOR THE PROPERTY SECTOR

Apportionment of costs and benefits between Landlords and Tenants

The Government will not legislate as to how to apportion the costs and benefits of the CRC between Landlords and Tenants. This is therefore an issue to be thrashed out commercially between the parties.

Landlords may be able to pass the costs of CRC onto their Tenants where leases permit. Both Landlords and Tenants would be well-advised to check the terms of their leases to see if this is the case. Where it is the case, it is likely that Tenants will want a share of the recycling payment. Negotiations around how that is to be calculated are proving to be contentious. Early attention to this issue in lease negotiations is recommended.

Early action rewarded

The Government has accepted that the Carbon Trust Standard should not be the only energy efficiency scheme which should be counted as “early action” (and so feed into the recycling payment). Accreditation to equivalent schemes, such as the Climate Change Agreement or EU Emissions Trading Scheme, will also count. In addition, “early action” will now receive greater weighting in assessing the recycling payment.

However, the carbon intensity of renewable energy will still not be differentiated from other energy sources.

Significant Group Undertakings (SGUs)

Subsidiaries large enough to qualify for the CRC in their own right will now be able to participate independently. Previously, these subsidiaries (formerly Principal Subsidiaries) would have participated as part of their holding company’s Group.

This could have significant implications for growing businesses in terms of the implications for the amount of the recycling payment.

Definition of “organisation”

An “organisation” under the CRC will still be determined (largely) according to parent-subsidary relationships rather than, for example, along operational or accountancy lines. An “organisation” therefore includes groups of companies where the total energy emissions of the whole group are taken into account for CRC purposes.

Concerns remain that this may prove to be complex to administer, particularly where a group of companies has a wide-ranging property portfolio comprising both office and heavy industrial use.

Next steps

The Environment Agency this month published guidance on registration for the CRC. This covers qualification requirements and the information required to be disclosed as part of the organisation’s registration. Registration for the CRC will be required from April 2010. A final draft CRC Order will be published towards the end of the year and will be in force in early 2010.

There is no doubt that the revised CRC remains a challenge for the property sector. Many Landlords and Tenants will be affected, whether directly as participants or indirectly, for example, as Tenants required to contribute to a Landlord’s CRC obligations.

It is recommended that all organisations check whether, and if so how, they are affected by the CRC in order to plan for its impact on their business.