GREENING THE TRADITIONAL COMMERCIAL LEASE: BUILDING A CASE FOR SUSTAINABLE COMMERCIAL REAL ESTATE THROUGH ECONOMICALLY PROFITABLE GREEN LEASES

ABSTRACT

Sustainability is in demand. The commercial real estate industry, however, has proven itself a slow-adopter of the green movement, which is quickly becoming the new normal. The result: (1) a lesson in the law of supply and demand; and (2) an opportunity. The businesses that fill commercial spaces generally understand the value of sustainability—both environmental and economic. Not surprisingly then, as they "green" their brands, the impact of sustainable real estate is not lost. While some investors wisely supply the demand for green spaces and reap the economic rewards of a sustainable real estate portfolio, others remain hesitant to commit to sustainability, turning a blind eye to the growing demand. Most hesitant investors—casual and expert alike—do not intentionally discount the business opportunity before them; they simply are uneducated about the green movement and its underlying economic incentives. The same can be said for those tenants who stand on the sidelines of sustainability.

For the legal practitioner frequently called on as a business adviser, this lack of education represents a tremendous opportunity to share with clients (building owners and tenants) the benefits of sustainable real estate and more importantly, the importance of a well-drafted green lease. This Note serves as a primer for practitioners new to the sustainable real estate frontier. Following an introduction to the commercial real estate industry and the green movement generally, the Note dismisses common misconceptions and highlights the economic incentives of sustainable real estate. After making a business case for green spaces, the Note turns to more substantive legal issues regarding commercial real estate leasing, including the net versus gross lease debate, structural drafting concerns, and specific green lease provisions. Finally, the Note concludes that in the absence of well-established jurisprudence or legislation, the only true means of protecting owners and tenants embarking on the path of sustainability is the law of contracts.

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I. INTRODUCTION

The commercial real estate market is in a slump.[1] Uncertain economic conditions have negatively impacted landlords, tenants, investors, and all those with ties to the building trades.[2] Despite this lull in growth, the awareness of and demand for environmental sustainability in the commercial real estate market is increasing as choosy commercial tenants, reveling in a buyer's market, look for the perfect space to call home.[3] Business savvy real estate owners and landlords recognize the demand for sustainable properties and wisely supply the market accordingly, to their benefit.[4]

Some owners and landlords, on the other hand, hesitate to embrace the "green" movement, avoiding the green lease at all costs.[5] There are several possible reasons for the avoidance, including (1) the cost of capital improvements; (2) the fear of never finding a return on invested capital; (3)

1. *See Commercial Real Estate Follows Home Values. Down.*, THE CHRISTIAN SCI. MONITOR (June 25, 2011), http://www.csmonitor.com/Business/Paper-Economy/2011/0625/Commercial-real-estate-follows-home-values.-Down ("[T]he nation's commercial property markets are continuing to slump through a tremendous downturn that has seen prices down some 48.95% since the peak set in October 2007.").

2. *See, e.g.*, BRACKEN HENDRICKS & MATT GOLDEN, TAKING ON THE TOOL BELT RECESSION: ENERGY EFFICIENCY RETROFITS CAN PROVIDE A REAL HELP FOR CONSTRUCTION UNEMPLOYMENT 1 (2010), *available at* http://www.americanprogress.org/wp-content/uploads/issues/2010/03/pdf/construction_jobs_memo.pdf ("Today, 2.1 million construction workers are out of a job. Jobs are down 38 percent since 2006 in residential construction alone. This 'tool belt recession' in the construction trades spills over to other parts of the economy as well. Because of declining demand for construction many manufacturing industry sectors that produce building products are currently operating at close to half their production capacity. As devastating as these numbers are, however, the unemployment figures for construction are likely an understatement of the problem due to the large number of self-employed construction workers that do not show up in payroll statistics, so the jobs picture is even more urgent than even these data suggest. Further, more than 90 percent of contractors in the construction industry are small businesses—another hard-hit segment of the economy.").

3. *See* PRICEWATERHOUSECOOPERS, LLP & URBAN LAND INST., EMERGING TRENDS IN REAL ESTATE 2013, at 31 (2013) [hereinafter EMERGING TRENDS IN REAL ESTATE 2013], *available at* http://www.uli.org/wp-content/uploads/ULI-Documents/Emerging-Trends-in-Real-Estate-US-2013.pdf.

4. *See id.*

5. *See* JONES LANG LASALLE, GLOBAL SUSTAINABILITY PERSPECTIVE 3 (2012), *available at* http://www.joneslanglasalle.com/GSP/en-gb/Documents/Global-Sustainability-Perspective-October-2012.pdf.

the work associated with creating, monitoring, and maintaining green spaces; and (4) the stigma of green building being an unnecessary and short-winded modern movement. Each of these reasons represents a legitimate, yet rebuttable, cause for concern.

The costs of going green need not be crippling and are easily justifiable: properly drafted contract terms can improve return on capital investments; the work required to create, monitor, and maintain green spaces can be unremarkable; and lastly, the green movement is not going away.[6] Indeed, the barriers to entry are often overstated, while the rewards are generally understated.[7] Moreover, lawmakers and market demand will continue to increase the legitimacy of green building year after year. It will soon become the industry standard, if it is not already, and those who fail to adapt will be added to the ever-growing list of market casualties.[8]

At the foundation of the green building movement, on the commercial real estate front, are the relationships between building owners and businesses that occupy such spaces. The contracts that document these relationships are called "green leases." A well-drafted green lease must benefit both owner and tenant while ensuring the environmental sustainability of the leased space.

II. THE INDUSTRY

A. *Scope*

To put the issue of green leasing into perspective and illustrate the overwhelming importance of the green movement, some statistics are in order. Note that the statistics also serve to counter the stigma that green building is merely a short-term, modern movement. To begin, there are

6. *See id.* ("It is . . . important for owners to look at other ways a sustainable investment can generate payback.").

7. *Compare, e.g.*, Carl J. Circo, *Should Owners and Developers of Low-Performance Buildings Pay Impact or Mitigation Fees to Finance Green Building Incentive Programs and Other Sustainable Development Initiatives?*, 34 WM. & MARY ENVTL. L. & POL'Y REV. 55, 55 (2009) (questioning why sustainable building practices need government encouragement if they are truly cost-effective), *with, e.g.*, JONES LANG LASALLE, *supra* note 5, at 3 (understating expected rewards by noting that "[o]wners/investors . . . don't expect 'windfall' profitability from going green").

8. *See* EMERGING TRENDS IN REAL ESTATE 2013, *supra* note 3, at 4 ("Office landlords should consider embracing flexible design features, green technologies, and Leadership in Energy and Environmental Design (LEED) systems or face the consequences.").

more than 80 billion square feet of commercial-sector floor space in the United States.[9] By 2035, there is expected to be nearly 110 billion square feet of such space—70% of which is to be new construction built after the year 2000.[10] For investors, these numbers represent enormous potential. For environmentally conscious regulators, however, these numbers are cause for great concern. This upward trend in commercial building is only one piece of the green building landscape. These commercial buildings are also a major source of resource consumption.

In 2008, the commercial sector consumed more than 18 quadrillion British Thermal Units (BTUs)—a 74% increase from 1980 levels.[11] Supplying energy to commercial buildings produced carbon dioxide emissions of more than 1,000 million metric tons in 2005.[12] Similar statistics can be found for a myriad of categories of usage, but suffice it to say commercial buildings represent a significant portion of energy costs in the United States.

The numbers evidence the sheer volume of commercial spaces and the part these spaces play in terms of total energy consumption. Because the commercial real estate market couples limitless opportunity and a steep growth rate with large-scale environmental concern, the issue of green leasing is ripe for discussion.

B. *The Past*

Sustainable building practices have been used for several millennia to increase energy efficiency and preserve resources. As early as the fifth century B.C., ancient Greeks established land use norms to this end, planning streets and buildings in a north-south orientation to maximize passive heating.[13] In the sixth century A.D., sunrooms became so common that the Romans established laws and judicial processes to ensure

9. D&R INT'L, LTD., 2010 BUILDINGS ENERGY DATA BOOK § 3.2, at 3-8 fig. 3.2.1 (2011), *available at* http://buildingsdatabook.eren.doe.gov/docs/DataBooks/2010_BEDB.pdf.

10. *Id.*

11. *Id.* § 3.1, at 3-1 fig.3.1.1.

12. U.S. ENERGY INFO. ADMIN., ANNUAL ENERGY OUTLOOK 2011, at 87 (2011), *available at* http://www.eia.gov/forecasts/archive/aeo11/pdf/0383(2011).pdf (detailing the United States' carbon dioxide emissions by sector and fuel type in 2005 and projecting emissions for 2035).

13. Borimir Jordan & John Perlin, *Solar Energy Use and Litigation in Ancient Times*, 1 SOLAR L. REP. 583, 585–86 (1979).

individual access to the benefits of solar resources.[14] With time, building standards improved and resources became scarcer. Out of necessity, energy preservation became more sophisticated. The nineteenth century saw structures like the Crystal Palace in London and Milan's Galleria Vittorio Emanuele II, both designed with sustainability in mind.[15] For example, the buildings incorporated roof ventilators and underground air-cooling chambers to moderate indoor air temperatures sustainably.[16] Early twentieth century New York City demonstrated the simplicity of sustainable innovation.[17] The New York Times Building, for example, used nothing more than deep-set windows to shade interiors from the sun.[18]

Builders continued to adopt innovative design in the name of efficiency, but it was not until the energy crises of the 1970s that the public at large accepted the need for an environmental movement.[19] In addition to the growing public awareness of environmental issues, skyrocketing oil prices "spurred significant research and activity to improve energy efficiency and find renewable energy sources."[20] This newfound awareness coupled with expanding knowledge in the field of energy led to the earliest experiments in contemporary green building and, subsequently, leasing.[21]

More recently, private interest groups and governments have taken on the role of green promoters. For example, the 1987 UN World Commission on Environment and Development, normally referred to as the Brundtland Commission, provided the first formal definition of "sustainable development."[22] In June 1993, at the International Union of

14. U.S. DEP'T OF ENERGY, THE HISTORY OF SOLAR 1, *available at* http://www1.eere.energy.gov/solar/pdfs/solar_timeline.pdf (stating that the Justinian Code established individual solar rights); Jordan & Perlin, *supra* note 13, at 592–93 (noting that the Romans used judicial decrees to settle disputes over solar access and providing examples of disputes).

15. BLDG. DESIGN & CONSTR., WHITE PAPER ON SUSTAINABILITY: A REPORT ON THE GREEN BUILDING MOVEMENT 4 (2003), *available at* http://www.usgbc.org/Docs/Resources/BDCWhitePaperR2.pdf.

16. *Id.*

17. *See id.*

18. *Id.*

19. *Id.*

20. *Green Building*, U.S. ENVTL. PROTECTION AGENCY, http://www.epa.gov/greenbuilding/pubs/about.htm (last updated Dec. 19, 2012).

21. *Id.*

22. G.A. Res. 42/187, ¶ 2, U.N. Doc. A/RES/42/187 (Dec. 11, 1987), *available at* http://www.un-documents.net/a42r187.htm; BLDG. DESIGN & CONSTR., *supra* note 15, at 5.

Architects and American Institute of Architects (UIA/AIA) World Congress of Architects, the two organizations executed the Declaration of Interdependence for a Sustainable Future.[23] This convention is widely seen as a historic crossroad in the green building movement.[24] The groups and their respective members committed themselves, on behalf of architectural and building-design professionals around the world, to

> [p]lace environmental and social sustainability at the core of [their] practices and professional responsibilities; [d]evelop and continually improve practices, procedures, products, curricula, services, and standards that will enable the implementation of sustainable design; [e]ducate . . . professionals, the building industry, clients, students, and the general public about the critical importance and substantial opportunities of sustainable design; [e]stablish policies, regulations, and practices in government and business that ensure sustainable design becomes normal practice; [and b]ring all existing and future elements of the built environment—in their design, production, use, and eventual reuse—up to sustainable design standards.[25]

At the same time, the U.S. Green Building Council (USGBC) was being established.[26] The USGBC is a 501(c)(3) nonprofit trade organization owned and operated entirely independently of the U.S. government "to improve the quality of life by transforming the design, composition, and operation of the places where we live, learn, work, and play within the short space of a generation."[27] The USGBC is perhaps best known for development of the internationally recognized Leadership in Energy and Environmental Design (LEED) green building program.[28]

The U.S. government also took advantage of the greening trend in the early 1990s. In 1992, the U.S. government adopted, for the first time, an energy policy act[29] complete with policies for building efficiency.[30]

23. BLDG. DESIGN & CONSTR., *supra* note 15, at 5.

24. *Id.*

25. UIA/AIA World Congress of Architects, *Declaration of Interdependence for a Sustainable Future*, CONTEXT INSTITUTE (June 18–21, 1993), http://www.context.org/about/definitions/.

26. *USGBC History*, U.S. GREEN BUILDING COUNCIL (2013), http://new.usgbc.org/about/history.

27. *Our Plan for Transformation*, U.S. GREEN BUILDING COUNCIL (2013), http://new.usgbc.org/about/strategic-plan.

28. *LEED*, U.S. GREEN BUILDING COUNCIL (2013), http://www.usgbc.org/leed.

29. Energy Policy Act of 1992, Pub. L. No. 102-486, 106 Stat. 2776 (1992).

Unofficial government adoption of the green movement, however, can be traced back to Earth Day 1993, when President Bill Clinton announced his intention to make the White House "a model for efficiency and waste reduction" and "a model for other Federal agencies, for State and local governments, for business, and for families in their homes."[31] The "Greening of the White House" project included several improvements, and it led to $300,000 in annual savings, as well as a reduction of atmospheric emissions to the tune of 845 tons of carbon per year.[32] The success of the project and the green movement in general also led to the issuance of three "greening" executive orders in 1998, 1999, and 2000.[33] Since these first political milestones, the U.S. government has continued to promote the cause of sustainability.[34]

C. *The Present*

Today, green building and the subsequent leasing of green space is increasingly becoming a best business practice for many of the largest retailers in the country.[35] Companies such as PNC Bank, Walmart, McDonald's, and Kohl's are a small handful of the hordes of businesses—large and small—committing to the green movement.[36] In fact, as of mid-

30. *Id.* §§ 101–106, 106 Stat. at 2782–94.

31. U.S. DEP'T OF ENERGY, GREENING OF THE WHITE HOUSE: SIX YEAR REPORT, at i (1999), *available at* http://clinton5.nara.gov/media/pdf/greening.pdf; *see also* BLDG. DESIGN & CONSTR., *supra* note 15, at 5.

32. BLDG. DESIGN & CONSTR., *supra* note 15, at 5.

33. *Id.* at 6; Exec. Order No. 13123, 3 C.F.R. 180 (2000); Exec. Order No. 13101, 3 C.F.R. 210 (1999); Exec. Order No. 13148, 3 C.F.R. 241 (2001).

34. *See, e.g.*, Energy Independence and Security Act of 2007, Pub. L. No. 110-140, §§ 431–441, 121 Stat. 1492, 1607–23 (2007) (codified as amended at 42 U.S.C. §§ 17001–17096 (Supp. 2009)) (setting goals and standards to reduce energy consumption in federally owned buildings).

35. *See* Andrew Martin, *Green Plans in Blueprints of Retailers*, N.Y. TIMES, Nov. 7, 2008, http://www.nytimes.com/2008/11/08/business/08build.html?pagewanted=all (describing the rising presence of green spaces owned by large retailers and the selfish motivations behind going green).

36. *See* Press Release, PNC Fin. Servs. Grp., Inc., U.S. Green Building Council Certifies 20 More PNC Green Branch Locations (Aug. 30, 2010), *available at* https://www.pnc.com/webapp/unsec/Requester?resource=/wps/wcm/connect/d86b2a00434b0fedad59fd87ce73677e/USGBC_Certies_082010.pdf?MOD=AJPERES&CACHEID=d86b2a00434b0fedad59fd87ce73677e (stating that the U.S. Green Building Council has certified ninety-seven PNC buildings, and that in 2002, PNC became the first major U.S. bank to design and build environmentally friendly LEED-certified bank branches in the United States); *Building Design*, KOHL'S CARES (2013), http://www.kohlsgreenscene.com/1-SustainableOperations/BuildingDesign.html

2012, more than two billion square feet of commercial floor space had been LEED-certified, and another seven billion square feet already registered for certification.[37] In short, "[g]reen is booming. Being green has become mainstream."[38]

III. THE PLAYERS

The primary player in the green building movement in the United States—sometimes even called the designer of the industry—is the USGBC.[39] Its internationally recognized green building certification system, LEED, "provides building owners and operators with a framework for identifying and implementing practical and measurable green building design, construction, operations and maintenance solutions."[40] The unique LEED certification process and its proprietary suite of rating systems are developed by balanced and transparent committees and technical advisory groups, and maintained by review of stakeholder comments, member ballot of new rating systems, and fair and open appeals procedures.[41]

Other certification systems used to certify or measure a building's sustainable qualities include Green Globes,[42] ENERGY STAR,[43] and

(recognizing Kohl's projects that embrace energy-saving designs and noting the chain's environmental-friendly building practices); Amanda Griscom Little, *Wal-Mart CEO Explains His Green Creed*, ENV'T ON NBCNEWS.COM (Apr. 14, 2006), http://www.nbcnews.com/id/12316725/#.US2CijBllQ2 (discussing Wal-Mart's desire to adopt green practices storewide); *The Road to Sustainability*, MCDONALD'S (2013), http://www.mcdonalds.com/us/en/our_story/values_in_action/the_road_to_sustainability.html (listing McDonald's rapidly expanding green practices).

37. Press Release, Ashley Katz, U.S. Green Building Council, LEED-Certified Building Stock Swells to Two Billion Square Feet Worldwide (July 26, 2012), *available at* http://www.usgbc.org/articles/leed-certified-building-stock-swells-two-billion-square-feet-worldwide.

38. *Strategic Plan 2009–2013: Executive Summary*, *in* USGBC ANNUAL REPORT (2008), *available at* http://communicate.usgbc.org/2008/ (follow the "Strategic Plan" hyperlink) (internal quotation marks omitted).

39. James W. Snavely, The U.S. Green Building Council: Designer of the Green Building Industry 1 (Winter 2007) (unpublished case study IR/PS CSR Case 07–09, University of California, San Diego), *available at* http://irps.ucsd.edu/assets/021/8420.pdf.

40. *LEED*, *supra* note 28.

41. *What Is LEED?*, U.S. GREEN BUILDING COUNCIL, N.C. CHAPTER, http://www.usgbcnc.org/?page=WhatIsLEED (last visited Apr. 11, 2013).

42. *The Practical Building Rating System*, GREEN GLOBES, http://www.greenglobes.com (last visited Apr. 11, 2013).

43. *The ENERGY STAR for Buildings & Manufacturing Plants*, ENERGY

BOMA.[44] Each rating system, including LEED, offers for a fee, a third-party building rating.[45] The rating serves as a measure of environmental success—a metric of sorts—for landlords, tenants, and anyone else interested in achieving or promoting sustainability.[46] The ratings are typically sought voluntarily to determine whether contracted-for levels of green design have been met after the construction process is complete.[47] For purposes of this Note, LEED certification will be used generally to refer to any of the third-party certifications that may be achieved.

IV. GREEN LEASING DEFINED

The beauty of the green lease is that it serves two masters—owners and tenants alike. For building owners, "an office building is a business, and the value of that business is based largely upon its ability to produce a desired return on investment."[48] To this end, a well-drafted green lease is essential to ensuring the owner a return on investment.[49] Green leases also benefit tenant-businesses by committing the building owner, or the contracted landlord, to green practices that would otherwise be the burden of the tenant.[50] With that as direction, a green lease can take many forms.

STAR, http://www.energystar.gov/index.cfm?c=business.bus_bldgs (last visited Apr. 11, 2013).

44. *BOMA 360 Program*, BUILDING OWNERS & MANAGERS ASS'N INT'L (2011), http://www.boma.org/getinvolved/boma360/Pages/default2.aspx.

45. *Id.* (basing application fees for certification on building square footage); *Frequently Asked Questions*, GREEN GLOBES, http://greenglobes.com/about-faq.asp (last visited Apr. 11, 2013) (estimating the typical cost of a Green Globes certification); *LEED*, *supra* note 28 (follow the "Learn more" hyperlink under the "How it works" heading); *The ENERGY STAR for Buildings & Manufacturing Plants*, *supra* note 43 (detailing application requirements for third-party certification, but noting there is no application fee).

46. *See BOMA 360 Program*, *supra* note 44; *Green Building Programs*, GREEN BUILDING INITIATIVE (2013), http://www.thegbi.org/green-globes/continual-improvement-for-existing-buildings.shtml (explaining the Green Globes rating system); *LEED*, *supra* note 28; *The ENERGY STAR for Buildings & Manufacturing Plants*, *supra* note 43.

47. *See* U.S. GREEN BLDG. COUNCIL, GREEN BUILDING RATING SYSTEM FOR EXISTING BUILDINGS: UPGRADES, OPERATIONS AND MAINTENANCE 2 (2004), *available at* http://www.usgbc.org/Docs/LEEDdocs/EB-final%20content%20version.pdf.

48. B. Alan Whitson, *Green Lease: Creating an Incentive to Effectively Design, Build and Manage High-Performance and Sustainable Buildings Through a Green Lease*, ENVTL. DESIGN & CONSTRUCTION, July 2006, at 15, *available at* http://www.centerforcorporatesustainability.org/pdf/article/8_25_06_Green_Lease.pdf.

49. *See id.*

50. *See* Celeste M. Hammond & Virginia M. Harding, *A Reminder that*

But, first and foremost, a green lease is just "a lease: a contract for the conveyance of real property for a term, in exchange for consideration of rent, that gives rise to a relationship of landlord and tenant."[51] One practitioner expanded upon the fundamental definition and gave this definition of a green lease: "a commercial lease that has been revised to clarify the specific green building requirements that are to be attained, to allocate the obligations and rights for achieving and maintaining the green building requirements, and to identify remedies or consequences for failing to comply with the various green building requirements."[52]

V. THE FIRST TAKEAWAY

The market shift to green building is now twenty years in the making, and it is gaining momentum. "Green building will soon be the rule rather than the exception."[53] Already, green building standards and incentives have been incorporated into legislation, executive orders, resolutions, ordinances, building codes, policies, and zoning practices across every level of government, as well as into privately established building covenants in planned communities.[54] In an effort to comply with federal, state, and local government mandates and to capture both the financial and environmental benefits of sustainability in this major market segment, the time to jump on the green leasing train is now. "Lawyers are on the front lines of lease negotiation and can lead change" once they recognize the importance of the green movement and the power they have to draft meaningful contracts in favor of their clients' unique interests.[55]

Green Buildings Need Green Leases, CHI. DAILY L. BULL., July 30, 2010, at 1, *available at* http://news.jmls.edu/wp-content/uploads/2010/07/CDLB-Hammond-Harding-Green-Building1.pdf.

51. Stuart D. Kaplow, *Does A Green Building Need A Green Lease?*, 38 U. BALT. L. REV. 375, 375 (2009) (citing BLACK'S LAW DICTIONARY 907 (8th ed. 2004)).

52. Larry Schnapf, *Green Building Leasing Issues: Commercial Leases Aren't Very Green Yet. But They Will Be, So Be Ready for the Change.*, PRAC. REAL EST. LAW., Nov. 2009, at 29, 36, *available at* http://www.srz.com/files/News/8f5d2513-02de-4abb-ab22-0ca0d27914fd/Presentation/NewsAttachment/84f3556f-5216-4d63-b7ec-0ee4d9ac7a44/Schnapf_Green_Building_Leasing_Issues_11_09_The_Practical_Real_Estate_Lawyer.pdf.

53. Kaplow, *supra* note 51, at 408.

54. *See* U.S. GREEN BLDG. COUNCIL, LEED PUBLIC POLICIES (2010), *available at* http://www.usgbc.org/Docs/Archive/General/Docs691.pdf; *see also* Schnapf, *supra* note 52, at 32–33.

55. S. Michael Brooks, *Green Leases and Green Buildings*, PROB. & PROP. MAG., Nov.–Dec. 2008, at 26, *available at* http://www.americanbar.org/publications/probate

VI. THE BUSINESS CASE FOR SUSTAINABLE COMMERCIAL SPACES

A. *The Obvious*

Although the green industry is clearly growing and the environment is in clear need of relief, the fact that this is a business issue is not lost. As previously recognized, commercial building owners and tenants are each in business.[56] Given the current economic stressors keeping businesses on their heels,[57] a client may mock the suggestion of going green and embrace the "price is king" philosophy.[58] To be sure, both parties to a commercial lease seek maximum return on investment, but the idea is not to burden one party more than another.[59] The idea is to achieve collaboration, or a partnership, whereby both parties are ensured an incentive for joining in a green relationship.[60] The discussion that follows embraces this concept and builds on a USGBC summary of the incentives owners and tenants receive for going green.[61] Once the incentives are established and both parties are sold on the concept, a green lease is the natural next step.

B. *Owner Incentives*

When compared to other commercial buildings of similar use and size, certified green spaces use less energy and produce fewer carbon dioxide emissions.[62] For some, such benefit to the environment is incentive enough.[63] For most, however, this is a fringe benefit at best.[64] To translate

_property_magazine_home/rppt_publications_magazine_2008_nd_brook.html.

56. *See* Whitson, *supra* note 48, at 15.

57. *See Commercial Real Estate Follows Home Values. Down.*, *supra* note 1.

58. *See* JONES LANG LASALLE, *supra* note 5, at 15.

59. *See* Hammond & Harding, *supra* note 50 (illustrating that green retrofits may burden landlords disproportionately).

60. *Id.* ("In the pre-green world, the [word] 'collaboration' was not an element in the landlord-tenant relationship. . . . The concept of a partnership or collaboration between a building owner and its tenants is a major change . . . .").

61. *The Business Case for Green Building*, U.S. GREEN BUILDING COUNCIL (July 27, 2012), http://new.usgbc.org/articles/business-case-green-building.

62. OFFICE OF APPLIED SCI., APPLIED RESEARCH, GSA PUB. BLDGS. SERV., ASSESSING GREEN BUILDING PERFORMANCE: A POST OCCUPANCY EVALUATION OF 12 GSA BUILDINGS 4 (2008) [hereinafter POST OCCUPANCY EVALUATION], *available at* http://www.gsa.gov/graphics/pbs/GSA_AssessGreen_white_paper.pdf (concluding that LEED-certified buildings use 26% less energy and produce 33% fewer carbon dioxide emissions).

63. *See* Kaplow, *supra* note 51, at 377 ("Green building is driven by . . . the environmental impacts of existing buildings." (citing MCGRAW HILL CONSTR., GLOBAL GREEN BUILDING TRENDS 20–21 (2008))).

environmental responsibility into something of persuasive monetary value, owners must step into the shoes of their tenants. Many lessees seeking to further their marketing reach and spur demand find significant value in corporate social responsibility (CSR) initiatives and are willing to pay a premium for spaces that earn them marketing points.[65] Owners should look beyond any skepticism of the infamous carbon dioxide and global warming debate to see the true business opportunity in green leasing—the opportunity to supply that which is in demand.

Still in the vein of satisfying tenant demand, owners may find incentive in higher occupant satisfaction rates.[66] Market research has shown up to 27% higher occupant satisfaction rates in green buildings.[67] By creating spaces that are attractive to tenants, building owners can lease spaces faster and reap the bottom-line benefits of increased occupancy rates.[68] Some industry reports boast occupancy increases of up to nearly 6.5% for new green construction and 2.5% for green renovations.[69] Such high occupancy rates, coupled with the low turnover rates that naturally follow, translate into profits for building owners.[70] After all, occupancy is the lifeblood of any lease-driven business model.

In addition to keeping spaces full, it has also been shown that green projects increase the value of buildings as much as 10%.[71] Rent increases follow similar trends, increasing more than 6% for new construction projects.[72] Compared to conventional commercial buildings, sustainably

64. *See id.* ("In another 2008 study, 47% of company executives said that cost savings were the leading driver for investment in energy efficiency, while only 16% were driven by environmental stewardship." (footnote omitted)).

65. MCGRAW HILL CONSTR., GREEN OUTLOOK 2011: GREEN TRENDS DRIVING GROWTH 11 (2010), *available at* http://aiacc.org/wp-content/uploads/2011/06/greenoutlook2011.pdf.

66. *See* POST OCCUPANCY EVALUATION, *supra* note 62, at 14.

67. *Id.*

68. *See* JONES LANG LASALLE, *supra* note 5, at 3 (summarizing building owners' expectations of better competitive advantage, greater demand for space, and increased occupancy after making sustainable property upgrades).

69. MCGRAW HILL CONSTR., *supra* note 65, at 11.

70. *Financial Benefits of Green Building*, COLLIERS INT'L (2013), http://www.colliers-sustainability.com/resources-information/financial-benefits-of-green-building/.

71. MCGRAW HILL CONSTR., *supra* note 65, at 11.

72. *Id.*; *see also* Schnapf, *supra* note 52, at 30 (noting that "certified buildings were able to command rent premiums of $11.24 per square foot over conventional buildings").

designed buildings also have 13% lower maintenance costs.[73] Unfortunately, the overall value of these statistical benefits is sometimes overlooked by present-thinking owners, concerned only with the immediate bottom-line. Indeed, the nearsightedness of some owners causes them to overlook the overwhelming proof that "minimal increases in upfront costs of about 2% to support green design would, on average, result in life cycle savings of 20% of total construction costs—more than ten times the initial investment."[74]

Owners cannot dispute that sustainability measures reap savings. Greg Kats, senior director for New York-based venture capital firm Good Energies, Inc., questioned the reasoning of all naysayers when he told the Wall Street Journal: "We now have a large enough, detailed enough body of data to say that the presumption is why wouldn't you do a green building?"[75] Still, there are those who would dispute the ability to recoup the costs of initial improvements. This raises one of the most common misconceptions in any green initiative: that the investment required to yield any measurable savings is prohibitive. To the contrary, it has been shown that an improvement as small as installing smart meters to put tenants on notice of usage can achieve significant reduction in consumption amounts.[76] Even if up-front costs are significant, contract structure, as discussed later, can alleviate the apparent imbalance between an owner's initial capital investment and the tenants' energy savings.[77]

Finally, for the hesitant owner, green building certification is a form of risk management. Certification provides a measure of protection against future lawsuits; it serves as third-party verification of measures taken by owners to go above and beyond the minimum standard of care—the

73. POST OCCUPANCY EVALUATION, *supra* note 62, at 4.

74. GREG KATS, THE COSTS AND FINANCIAL BENEFITS OF GREEN BUILDINGS: A REPORT TO CALIFORNIA'S SUSTAINABLE BUILDING TASK FORCE, at ii (2003), *available at* http://www.calrecycle.ca.gov/greenbuilding/design/costbenefit/report.pdf.

75. Sari Krieger, *Half of Non-Residential Buildings Will Be Green By 2015—Study*, WALL ST. J. VENTURE CAP. DISPATCH BLOG (Jan. 6, 2010, 4:30 PM), http://blogs.wsj.com/venturecapital/2010/01/06/half-of-non-residential-buildings-will-be-green-by-2015-study/ (quoting Greg Kats) (internal quotation marks omitted).

76. *See, e.g.*, Tibi Puiu, *Dubuque, USA Leads the Way for the Smart Cities of the Future*, ZME SCI. (Nov. 4, 2011), http://www.zmescience.com/science/dubuque-usa-leads-the-way-for-the-futures-smart-city-infrastructure/ (discussing reductions in consumption levels made recently through a program established by Dubuque, Iowa officials and IBM).

77. *See infra* Part VII.B.2.a.

building code.[78] Also, given the red-tape delays that frequently stall or close the door on development projects, faster permitting and special permit assistance given to green projects can be considered a type of risk mitigation.[79] One example of risk mitigation and its underlying financial benefit can be found in Austin, Texas. The city fast-tracked the green development of a large retailer, causing the owner to open one full year ahead of schedule.[80] The special treatment created a $2.8 million profit for the owner—enough to pay for the entire cost of the building.[81] The faster sale and leasing of green real estate is also a risk management benefit to owners in the sense that owners investing in green building are likely less susceptible to the financial risk of stagnant real estate markets.

C. *Tenant Incentives*

One tenant incentive, discussed in part above, is the competitive social advantage that results from the commitment to green initiatives.[82] Studies have shown that more than 60% of today's business leaders are committed to sustainability, not because they anticipate government regulation or because they hope to recoup energy costs, but because social responsibility leads to market differentiation and improved financial performance.[83]

Not only does green building play a part in each tenant's implied duty of social responsibility, but it also yields many public relations benefits. For example, Adobe was hailed as a green leader when it announced in 2006 that it became the first to receive three Platinum LEED ratings from the USGBC;[84] PNC Financial Services made headlines when it announced it

78. *The Business Case for Green Building*, *supra* note 61.

79. *Id.*

80. JERRY YUDELSON, THE GREEN BUILDING REVOLUTION 35–36 (2007) (citing personal communications of S. Richard Fedrizzi, CEO, U.S. Green Building Council).

81. *Id.*

82. JONES LANG LASALLE, *supra* note 5, at 3; EMERGING TRENDS IN REAL ESTATE 2013, *supra* note 3, at 56 ("Green buildings with high ratings . . . and energy-efficient systems leapfrog the competition: tenants calculate operating savings and find they can attract young talent who favor 'cool space' and nods by their employers to environmental correctness.").

83. MCGRAW HILL CONSTR., *supra* note 65, at 10.

84. Press Release, Adobe Sys. Inc., Adobe Headquarters Awarded Highest Honors from U.S. Green Building Council (Dec. 5, 2006), *available at* http://www.adobe.com/aboutadobe/pressroom/pressreleases/pdfs/200612/120506LEED.pdf; *The Business Case for Green Building*, *supra* note 61.

was building the world's greenest skyscraper;[85] PepsiCo's Frito-Lay claimed eight LEED Gold certifications for existing buildings;[86] and even the Red Cross of Cincinnati, a nonprofit corporation, boasts a LEED-certified headquarters.[87]

A closer study of the companies that have made the move to sustainable spaces illustrates further incentives. First, lower operating costs make return on investment a short-term goal.[88] Adobe invested approximately $650,000 to retrofit its property in 2001, and in only five years, the improvements already produced a return on investment of almost 115%.[89] The Cincinnati chapter of the Red Cross saw similar returns.[90] By replacing its previous headquarters and disaster operations center with a new green building, the Red Cross gained more than 10,000 square feet of space while also cutting energy costs and freeing up substantial amounts of capital resources.[91] Because green buildings can provide useful consumption metrics—as evidenced by the foregoing data—green tenants are able to benchmark their energy usage and consciously make reductions to save money year after year.[92] Many tenants appropriately view green buildings as a tool to reduce costs during these challenging economic times.[93]

Second, sustainable spaces are happier, more productive spaces.

85. Press Release, PNC Fin. Servs. Grp., Inc., PNC Announces Plans for World's Greenest Skyscraper (May 23, 2011), *available at* http://multivu.prnewswire.com/mnr/pnc/42893.

86. Press Release, Frito-Lay N. Am., Inc., PepsiCo's Frito-Lay Modesto Facility Celebrates Becoming California's First Existing Food Manufacturing Site to Achieve LEED® Gold (May 26, 2011), *available at* http://www.fritolay.com/about-us/press-release-20110526.html.

87. *Locations: Cincinnati Area Chapter*, AM. RED CROSS, http://www.redcross.org/oh/cincinnati/about/locations (last visited Apr. 12, 2013).

88. *See* MCGRAW HILL CONSTR., *supra* note 65, at 11 (noting significant improvement in return on investment after undertaking green projects).

89. Press Release, Adobe Sys. Inc., *supra* note 84.

90. *See* Chuck Saletta, *Going Green Is More Than Just Good PR*, DAILY FIN. (Aug. 3, 2011), http://www.dailyfinance.com/2011/08/03/going-green-is-more-than-good-pr/.

91. *Id.*

92. B. Alan Whitson, *Turning Green into Gold: Proper Metrics Key to Measuring Performance of Green Buildings*, OFFICEINSIGHT (Officeinsight, New Canaan, Conn.) Feb. 25, 2008, at 8–9, *available at* http://www.centerforcorporatesustainability.org/pdf/article/Metrics_Key_to_Measuring_Green_Performance.pdf; *see also* Puiu, *supra* note 76; *supra* note 76 and accompanying text.

93. Martin, *supra* note 35.

Whether it is the aesthetic appeal of a fresh green design or improved indoor air quality, research shows that occupants of green buildings are generally more satisfied than occupants of other similar properties.[94] So, just as owners have an easier time keeping tenants in green buildings, tenants should have an easier time keeping employees in green buildings—and they do.[95] Reducing turnover lowers recruiting and training costs and creates operational efficiencies that, in turn, save tenants money.[96] Tenants also find incentive in harder working employees. Employees working in sustainable buildings reported productivity increases of forty hours per year.[97] Consider the fact that the Environmental Protection Agency (EPA) estimates that sickness caused by poor lighting and poor indoor air quality—both remedied in most green designs—costs U.S. businesses some $60 billion annually.[98] With numbers that high, and the fundamental assumption that human resources are usually a tenant's largest expense,[99] a reasonable argument can be made that the greatest incentive for tenants to go green is not energy savings or an enhanced public image, but improved human capital.[100]

VII. THE LEASE

A. *Generally*

1. *A Hybrid Approach*

Assuming both parties have agreed to come together as partners in a green building, we turn to the contract that will define the relationship—the green lease. The contract will bind both parties to comply with certain

94. POST OCCUPANCY EVALUATION, *supra* note 62, at 14.

95. *Financial Benefits of Green Building*, *supra* note 70.

96. *Id.* (stating that the cost of voluntary employee turnover is between $30,000 and $50,000 per incident).

97. MCGRAW HILL CONSTR., *supra* note 65, at 11.

98. Andrew Sibley, *IAQ and Occupational Asthma*, OCCUPATIONAL HEALTH & SAFETY (Apr. 1, 2012), http://ohsonline.com/Articles/2012/04/01/IAQ-and-Occupational-Asthma.aspx.

99. JEFF HIGGINS & GRANT COOPERSTEIN, HUMAN CAPITAL MGMT. INST., MANAGING AN ORGANIZATION'S BIGGEST COST: THE WORKFORCE 2, *available at* http://www.hcminst.com/files/OrgPlus_Total_Cost_Workforce_.pdf; *see also Financial Benefits of Green Building*, *supra* note 70 ("On average, salaries and benefits account for 70-80% of a company's expenses compared to rent at 5% and energy at 1-2%.").

100. *Financial Benefits of Green Building*, *supra* note 70 ("[W]orker productivity gains and human capital cost savings can result in substantial bottom-line savings, even greater savings than energy cost reductions.").

sustainability standards and create contract mechanisms whereby each party can find the return on investment they seek.[101]

The most important lease concept relevant to this discussion is that of the gross versus net lease. In a gross lease, the tenant pays a set sum or gross amount for rent, while the landlord pays all other expenses.[102] The past several decades have seen gross leases decline in popularity.[103] In the now commonly used net lease, the tenant pays a set sum for rent plus an additional amount for utilities, property taxes, insurance, etc.[104] Under a net lease, the landlord would then only pay for maintenance, repairs, and the balance of any taxes or insurance not paid by the tenant. Modern variations on the net lease include the double-net lease, and the more common, triple-net lease.[105] The more "net" the lease, the more the tenant pays and the less burdened the landlord becomes, often covering only the costs of large structural repairs.[106] The details of these variations are not as important as the fundamental concept that over time landlords have shifted more and more of the financial burden of post-construction operating expenses to tenants via a net-lease contract.[107]

The rise of the green building in a net-lease world has created what is referred to as the "split incentive" problem: the landlord ponies up all the risk and invests all the capital to make sustainable improvements, but the tenant receives all the benefits and savings associated with reduced consumption.[108] To a landlord, the net lease offers zero return on investment—a significant disincentive to act sustainably.[109] Conversely, the gross lease creates a significant disincentive for tenants to reduce

101. *See* Whitson, *supra* note 48, at 18.

102. BLACK'S LAW DICTIONARY 971 (9th ed. 2009) (defining gross lease).

103. *See* B. ALAN WHITSON, LEASE STRUCTURE HINDERS ENERGY EFFICIENCY (2005), *available at* http://www.squarefootage.net/pdf/article/ENERGY_LeaseStructureHinders.pdf; Whitson, *supra* note 48, at 16.

104. BLACK'S LAW DICTIONARY, *supra* note 102, at 972, (defining net lease).

105. *See id.* (defining net-net-net lease).

106. *See* WILLIAM L. VENTOLO, JR. & MARTHA R. WILLIAMS, FUNDAMENTALS OF REAL ESTATE APPRAISAL 319 (8th ed. 2001).

107. Whitson, *supra* note 48, at 15–16.

108. Stephen R. Miller, *Commercial Green Leasing in the Era of Climate Change: Practical Solutions for Balancing Risks, Burdens, and Incentives*, 40 ENVTL. L. REP. 10,487, 10,498 (2010) (internal quotation marks omitted).

109. Peter Friedenberg, *Key Provisions of a Green Lease*, GREEN DEV. NEWS (Nat'l Ass'n of Indus. & Office Props., Herndon, Va.), Apr. 2009, *available at* http://www.sherin.com/D6C897/assets/files/Documents/PF_Key_Provisions_of_a_Green_Lease.pdf.

consumption or act sustainably; when all the energy costs fall upon the landlord, the tenant has no skin in the game.[110] To resolve this split incentive and level the playing field, green buildings require a compromise, something not traditionally a part of the landlord–tenant relationship.[111] The compromise will be a hybrid lease that balances the incentives of the net and gross leases.[112]

A solid grasp of the gross versus net lease distinction becomes particularly important when upgrading high-demand buildings that were not initially designed to meet green standards, such as the Empire State Building.[113] Existing building owners, unless at the end of a lease term, do not have the luxury of starting over with new construction, new tenants, and a new hybrid lease. Instead, they must work with current tenants to tweak the existing net or gross lease into something more green. "The portion of the green building movement that involves retrofitting existing buildings will be successful only if a new 'partnership' between landlords and tenants can be achieved . . . ."[114]

After the net versus gross wrinkle is ironed out and the disincentives are neutralized, what will this hybrid lease look like? S. Michael Brooks suggests two models: (1) a "paternalistic" lease, which reduces consumption requirements and allows responsible green behavior to be dictated by one party, either the tenant or the landlord; or (2) a "cooperative" lease, which allows parties to agree on mutual objectives together and use the lease to set out the responsibilities and liabilities of each party.[115]

The one-sided paternalistic approach will be tenant- or landlord-driven, depending on the environmental or financial motivation of the parties.[116] A tenant-paternalistic lease is driven by the goals of a take-

110. *Id.*

111. Hammond & Harding, *supra* note 50.

112. Friedenberg, *supra* note 109.

113. *See, e.g.*, Press Release, Jones Lang LaSalle, Empire State Building Achieves LEED Gold 1 (Sept. 13, 2011), *available at* http://www.usgbc.org/ShowFile.aspx?DocumentID=10266. In 2011, after a $550 million renovation, the eighty-year-old, 2.85 million square foot building, achieved LEED certification. *Id.* The building's energy consumption is expected to be reduced by more than 38%, which should save $4.4 million annually—enough to break even in only three years (based on the cost of implementation). *Id.* The building also achieved ENERGY STAR certification. *Id.*

114. Hammond & Harding, *supra* note 50.

115. Brooks, *supra* note 55.

116. *See id.*

charge tenant.[117] Such a tenant could be one with a strong green brand or one responsible for internal green targets.[118] Conversely, a landlord-paternalistic lease is driven by a landlord who "wants to green its portfolio . . . or be seen as environmentally responsible, and wants its tenants to toe the line to achieve certain environmental goals."[119]

The cooperative model would exist when both parties buy into the need to go green and when both want to be sure the goal is achieved.[120] Regardless of the lease approach adopted by the parties, a green lease can include provisions for as many or as few green targets and initiatives—and accompanying liabilities—as the parties can contemplate, negotiate, or make economically viable.[121]

2. *The Structure*

The structure of any green lease depends largely on the complexity of the green provisions to be incorporated. When the leasing relationship and physical characteristics of the building are simple and the green objectives are straightforward, a green lease can be structured as a simple addendum to a traditional lease.[122] For moderately complex circumstances, a number of specific green provisions can be incorporated into the body of a traditional lease.[123] Admittedly, this is more work than an addendum, but by including the green language in the lease itself, both parties acknowledge that sustainability is not merely an afterthought; instead, sustainability becomes a central feature of the overall agreement. A third approach to structuring a green lease is to create a new green lease entirely.[124] A new green lease, carefully tailored to the objectives of the contracting parties and the building at issue, is the most comprehensive approach because it suggests total commitment to sustainability.

117. *See id.*
118. *Id.*
119. *Id.*
120. *Id.*
121. Michael Singer, *Green Lease*, PLI'S POCKET MBA, Aug. 12, 2008, *reprinted in* POCKET MBA 3: EVERYTHING AN ATTORNEY NEEDS TO KNOW ABOUT FINANCE 243, 246 (2009).
122. Ronald B. Grais & Kristen M. Boike, *Jenner & Block: Green Leasing—The Changing Environment of Leasing*, EMERGING ISSUES COMMENT. (Jenner & Block, Chi., Ill.), June 2008, at 5, *available at* http://jenner.com/system/assets/publications/759/original/Green_Leasing-Intro_Article.pdf?1313782288.
123. *Id.*
124. *Id.*

For parties that elect to forgo a formal certification system, such as LEED, and instead seek to devise their own standards, the attachment method is generally sufficient.[125] For those parties that are serious about green and invest in third-party certification, however, green standards should at least be incorporated into the lease itself.[126]

With the most suitable structure in mind, practitioners should have no problem finding a starting point. Many trade organizations and do-good practitioners have attempted to standardize the green lease drafting process by providing sample addenda and lease templates.[127] The content varies, and the approaches are each unique, so it is important to remember that there is not a one-size-fits-all approach to drafting a green lease.[128] This is no surprise considering the myriad factors that might affect a green lease relationship, such as whether the lease is landlord- or tenant-driven or cooperative, the size of the building, the age of the building, the goals of the parties, certification requirements, the green technology incorporated into the building, geographic factors, local zoning requirements, and the term of the relationship, to name a few.[129] To use the available resources most effectively, a drafting attorney must remember that it is "the expansion of knowledge, not merely the propagation of forms, [that] is the key to success."[130]

125. Miller, *supra* note 108, at 10,496.

126. *Id.*

127. For example, The Real Property Association of Canada (REALpac), the Building Owners and Managers Association (BOMA Green Lease Guide), the Natural Resources Defense Council (Lease Energy Efficiency Guide), the California Sustainability Alliance (Green Leases Toolkit), and the USGBC (Green Office Guide) have all made green lease templates, lease riders and addenda, or forms available for download or purchase. CTR. FOR MKT. INNOVATION, NATURAL RES. DEF. COUNCIL, ENERGY EFFICIENCY LEASE GUIDANCE 1–13 (2011), *available at* http://www.nrdc.org/greenbusiness/cmi/files/CMI-FS-Energy.pdf; REAL PROP. ASS'N OF CAN., GREEN LEASE GUIDE: FOR COMMERCIAL OFFICE TENANTS, app. B at 65–71 (2010), *available at* http://c.ymcdn.com/sites/www.realpac.ca/resource/resmgr/docs/greenleaseguidefinal05feb10.pdf; *Green Leases Toolkit*, CAL. SUSTAINABILITY ALLIANCE, http://sustainca.org/green_leases_toolkit (last visited Apr. 11, 2013); *Green Office Guide: Integrating LEED Into Your Leasing Process*, U.S. GREEN BUILDING COUNCIL (2013), http://www.usgbc.org/resources/green-office-guide-integrating-leed-your-leasing-process; *New BOMA Green Lease Guide Offers Solutions for Writing Sustainability into Lease Agreements*, BUILDING OWNERS & MANAGERS ASS'N INT'L (June 22, 2008), http://www.boma.org/Resources/news/pressroom/Pages/press062208-3.aspx.

128. Grais & Boike, *supra* note 122, at 4.

129. *See id.* at 4–5.

130. STEVEN A. TEITELBAUM & BRYAN J. DARDIS, CURRENT DEVELOPMENTS IN GREEN LEASING 8, *available at* http://www.americanbar.org/content/dam/aba

B. The Terms

1. *Importance Thereof*

The ultimate goal of green leasing is a symbiotic relationship between the owner and tenant.[131] The terms of the lease should be drafted carefully with that end in mind, but it is not always a simple task. Because no two parties ever see exactly eye-to-eye, the owner and tenant almost certainly will bring unique interests to the negotiating table.[132] Often times, "[s]ustainability, and the willingness to pay for costs associated with sustainability, may be more important to one party than the other."[133]

More predictable yet, are conflicts over control. For example, a tenant might disagree with a landlord's decision to control the type of cleaning supplies used in the leased space, the hours of operation, or the thermostat settings.[134] The landlord, however, might have a good reason for regulating operations, for example, to achieve a particular level of indoor air quality or to minimize energy consumption.[135] In an existing building, a long-time tenant might have an equally hard time convincing a stubborn landlord to change his or her old ways in order to accommodate the tenant's newfound commitment to sustainability.[136] With mixed motives and on-and-off cooperation constantly threatening the success of every green leasing relationship, practitioners cannot afford to underestimate the uniting power of a well-drafted green lease.[137]

Because the green building movement is so young, very little case law exists to interpret green lease relationships.[138] Unlike parties to other contracts, in which gap-fillers regularly serve to fill in terms either

/events/real_property_trust_estate/symposia/2010/1945.authcheckdam.pdf.

131. *See* Hammond & Harding, *supra* note 50 (describing this symbiotic relationship as a partnership).

132. *See* Grais & Boike, *supra* note 122, at 5 (explaining that owners and tenants occupy the same space, but rarely share the same environmental consciousness or financial incentive).

133. *Id.*

134. *Id.*

135. *Id.*

136. *Id.*

137. *See* Whitson, *supra* note 48, at 18 (listing ten essential elements for practitioners to keep in mind when drafting a green lease).

138. Kaplow, *supra* note 51, at 400 ("Green leasing language is new and untested, unlike traditional commercial lease forms, which . . . ha[ve] been interpreted by American courts for hundreds of years.").

forgotten or intentionally left out,[139] parties to green leases cannot rely on the courts for interpretation. Neither can they wait for legislatures to agree on sustainability standards.[140] To mitigate risk to the fullest extent possible, lawyers should seek to draft comprehensive leases.[141] Because a perfectly comprehensive lease is impossible to draft, or at least financially infeasible, a comprehensive lease for purposes of this discussion means a lease that leaves as little room as possible for client disappointment in the event one party attempts to renege on its commitment to sustainability. A comprehensive green lease then effectively becomes an insurance policy upon which parties can rely in the absence of black letter law.[142]

2. *Specific Provisions*

The following is a list of several common green lease provisions. It is not intended to serve as an exhaustive summary of provisions, but rather a sample of the special attention these leases demand.[143] For the prudent drafter, every provision, without exception, is an opportunity to exercise the freedom of contract and further the objectives of the client.

a. *Cost structure*. The most important provision of the contract is likely the cost structure that will govern the parties' relationship. The hybrid approach and the net and gross lease mechanisms discussed above are applied here.[144] Most lease transactions are structured as net leases.[145] The reasons for the switch from gross to net leases are beyond the scope of this Note, but proponents of the net lease say it leads to a more transparent

139. For example, Article 2 of the Uniform Commercial Code provides default terms such as price, delivery, warranty, risk of loss, and others—all to ensure that no contract for the sale of goods fails. *See* U.C.C. § 2-305 (2010) (discussing open price terms); *id.* §§ 2-307 to -308 (discussing the method and location of delivery of goods); *id.* §§ 2-312 to -318 (discussing warranties); *id.* § 2-303 (discussing the allocation or division of risks). Real estate contracts, on the other hand, do not have a statutory compilation of default terms. Instead, the agreement between contract parties is strictly that which is expressly incorporated into the lease documents.

140. Nor should they. Kaplow, *supra* note 51, at 400 ("Green leasing law is in its infancy and thus presents a tremendous opportunity for innovative thinking.").

141. *See id.* at 400–07 (proposing several important issues to address in green leases).

142. *See id.* at 400.

143. *See id.*

144. *See supra* Part VII.A.1.

145. Schnapf, *supra* note 52, at 37.

arrangement.[146] That may be the case, but green building requires capital, and capital comes from owners.[147] That makes owners priority number one. Although incentives are in place for owners to join the green building movement without it,[148] the gross lease must return—at least in part—in order to maximize the willingness of owners to invest in sustainable real estate.[149] Hence, the hybrid lease that best facilitates collaboration should be substantially in the form of a gross lease.[150] One approach is to use what is called a modified gross lease, in which the tenant pays a base amount of operating expenses and taxes when the lease begins and then the base amount plus any annual escalations over the base amount in subsequent years.[151] This hybrid approach provides tenants an incentive to conserve and gives landlords an incentive to invest their capital.[152] To balance the inequities further, the modified gross lease should also provide for the pass-through of capital improvements on an amortized basis.[153]

This is only one possible solution. Most scholars and practitioners, regardless of their bias toward net or gross leases, generally agree that all lease structures can be made equally green.[154] As long as both contracting parties agree to the cost structure and find themselves sufficiently incentivized to keep the project green, any cost structure will work.

b. *Define green.* While the cost structure is arguably the most important provision in the lease, at the end of the day, every green lease should define what each contracting party means by "green."[155] Each party enters into a lease agreement with unique motives, and in a green lease, each will have unique sustainability goals and standards.[156] It goes without

146. Whitson, *supra* note 48, at 16.
147. *See* JONES LANG LASALLE, *supra* note 5, at 3.
148. *See supra* Part VI.B.
149. Whitson, *supra* note 48, at 18.
150. *See id.*
151. Friedenberg, *supra* note 109.
152. *See id.*
153. *Id.*
154. John M. Sharp, *"Green" Leasing: A Practitioner's Overview*, REAL PROP., PROB. & TRUST SEC. NEWSL. (Wash. State Bar Ass'n, Seattle, Wash.), Summer 2009, at 7, *available at* http://www.stoel.com/files/Green%20Leasing%20Article%20-%20J.Sharp.pdf.
155. Andrea Carruthers, *Crafting a Green Lease*, MINN. LAW., Sept. 2008, at S-5, *available at* http://www.faegrebd.com/webfiles/Green%20Lease.pdf.
156. Grais & Boike, *supra* note 122, at 5.

saying, but without defining the exact expectations of the parties, it is impossible to be certain the contract is properly drafted to satisfy both parties' objectives. Whether green is defined broadly or narrowly, having it defined upfront serves to frame the remaining provisions of the lease.[157]

c. *Performance standards.* Targets and benchmarks flow from the parties' definition of green. The green targets and benchmarks should be spelled out in the lease with as much detail as possible.[158] Performance standards or technical goals are the heart of the green lease, and they act as the means whereby the targets and benchmarks are achieved.[159] Performance standards can be created to regulate things such as lighting, indoor air quality, recycling, water use, heating, ventilation, and air conditioning (HVAC), and more.[160] These specific how-to standards are the topic of vast amounts of green literature and are too complex to explore in a few short paragraphs. For purposes of this Note, it is enough to say that performance standards keep a building sustainable, however the term is defined between the parties to the lease.[161]

d. *Right of entry and audit.* Most commercial leases allow a landlord access to a tenant's space to perform necessary maintenance.[162] Beyond routine maintenance calls, however, access is usually limited to emergencies only.[163] A well-drafted green lease will expand the right of entry to permit the landlord access to the tenant's property for those green purposes "that may be necessary or proper to implement the landlord's sustainability practices and otherwise maintain any third-party Green certification."[164] Without an expanded right of entry, landlords are powerless in terms of ensuring compliance with the performance standards agreed to by the parties.[165] As landlords push for an expansion of the right of entry, wise tenants will rightfully seek to maximize privacy rights and

157. Miller, *supra* note 108, at 10,496–97 (describing competing green leases and the importance of paying particular attention to the clients' objectives when determining the breadth of any provision's applicability).

158. Brooks, *supra* note 55.

159. *Id.*

160. *Id.*

161. *See* Miller, *supra* note 108, at 10,497.

162. Schnapf, *supra* note 52, at 39.

163. *Id.*; *see also* Kaplow, *supra* note 51, at 405.

164. Kaplow, *supra* note 51, at 405 (internal quotation marks omitted).

165. *See* Schnapf, *supra* note 52, at 39.

minimize landlord access. To effectively maintain a green relationship, tenants should concede the point and allow regularly scheduled inspections to be incorporated into the lease, yet leverage the concession by insisting on a reciprocal right of audit.[166] Depending on the cost structure of the lease, a right-to-audit clause can protect the tenant from overcharges by gaining the right to audit the landlord or other tenants in a multi-tenant building regularly.[167] After all, the green lease relationship must be a partnership.[168]

e. *Maintenance.* Maintenance provisions are very common in green leases. These provisions should detail the materials, procedures, and protocols of building maintenance.[169] For example, cleaning materials might be limited to only those that satisfy the Green Seal GS-37 standard.[170] The timing of maintenance could also be addressed.[171] When possible, it should be agreed that all maintenance be completed during business hours to limit energy consumption after hours.[172] When third-party contractors are used for regular maintenance, parties to the lease might also want to agree on policies to ensure the contracted-for tasks are being completed using sustainable practices.[173]

f. *Recycling/waste management.* Green leases should always contain provisions regarding recycling and waste management.[174] This provision should require compliance with both local law and agreed upon standards of waste management.[175] A waste stream audit, a valuable sustainability tool for both landlord and tenant, is also becoming standard green lease content.[176]

166. Whitson, *supra* note 48, at 18.
167. *See id.*
168. Hammond & Harding, *supra* note 50.
169. Whitson, *supra* note 48, at 18.
170. Kaplow, *supra* note 51, at 406–07.
171. Miller, *supra* note 108, at 10,497.
172. *See id.*
173. *Id.*
174. *See id.* at 10,497–98; *see also* Eric A. Kremer & Carmela D. Nicholas, *"Green" Leasing: Landlord and Tenant Perspectives*, PERSP. ON REAL EST. NEWSL. (Pillsbury Winthrop Shaw Pittman LLP, New York, N.Y.), Spring 2012, at 1, 3–4, *available at* http://www.pillsburylaw.com/siteFiles/Publications/RealEstateNewsletterSpring2012.pdf (providing sample lease language covering this topic).
175. Miller, *supra* note 108, at 10,497–98.
176. Kaplow, *supra* note 51, at 405.

g. *Construction, alternation, and repair.* These provisions require compliance with green standards should build-out, remodeling, or maintenance be conducted by the tenant.[177] Mutual covenants could likewise hold the landlord responsible for compliance with green standards if the landlord is responsible for the work.[178] Because third parties are often used in the construction process, measures should also be taken to extend green standards to them.[179]

h. *Annual performance report.* An annual performance report will allow each party to hold the other accountable for the sustainability objectives agreed upon at the beginning of the lease term, as well as for compliance with the more detailed performance standards set out in the lease.[180] For a simple lease, the annual report may require nothing more than a simple e-mail exchange, but for more complicated leases with certified spaces, the report should be much more comprehensive.[181] It might even require an annual meeting to facilitate a walk-through, data-sharing, or a third-party audit.[182]

i. *Insurance requirements*. Insurance for any green building should account for its peculiar value-added features.[183] This value includes both the value of green technology incorporated into the space and the value of any building certification.[184] Green technology, including specially designed HVAC systems, is almost always more expensive than traditional technology.[185] This additional cost needs to be reflected in the insurance policies required under the lease.[186] Further, if a building that has been third-party certified by LEED, Energy Star, or Green Globes, for example, is destroyed, the building owner would want to be confident the insurance values are sufficient to restore the building to its prior standard, including

177. *Id.* at 402–03; Miller, *supra* note 108, at 10,498–99.
178. *See* Kremer & Nicholas, *supra* note 174, at 4 (recommending reciprocal covenants).
179. Kaplow, *supra* note 51, at 403.
180. Miller, *supra* note 108, at 10,499.
181. *See id.*
182. *Id.*
183. Grais & Boike, *supra* note 122, at 6.
184. *Id.*
185. *Id.*
186. *Id.*

the cost of recertification.[187] Several insurance companies are beginning to offer products tailored to green buildings.[188] In addition to replacement coverage, these custom policies cover everything from recertification to crisis management consultant costs, all at lower-than-average premiums.[189]

j. *Dispute resolution for noncompliance.* As discussed previously, judicial remedies for breach of green leases are not well-established due to a lack of industry litigation.[190] Therefore, the consequences of failure by either party to comply with agreed-upon objectives, provisions, or certification requirements, must be expressly added to the lease. This is a balancing act, however, as the remedies must not be so harsh as to deter parties from agreeing to the lease in the first place. As with most industries, the building industry has turned to alternative dispute resolution methods such as arbitration or mediation to address conflict.[191] Some green leases require the arbitrator or mediator to be "a LEED[-]Accredited Professional."[192] For properties not certified by a third party, the arbitrator or mediator may not need to be accredited, simply because the disputed provisions will likely be fairly generic in nature.[193] Other issues worth addressing in this provision are whether the decision of the arbitrator or mediator is binding and whether or not the costs and attorney's fees are recoverable.[194]

k. *Future risk*. Risk allocation is another important issue to be addressed in every green lease.[195] Future regulations, incentives, and changes to third-party rating systems will almost certainly affect green buildings at some point.[196] Such changes may force building owners and

187. *Id.*

188. Andrew C. Burr, *Top 10 Green Building News Stories of 2008*, COSTAR GROUP (Dec. 30, 2008), http://www.costar.com/News/Article/Top-10-Green-Building-News-Stories-of-2008/108858.

189. *Id.*; *see also* YUDELSON, *supra* note 80, at 36.

190. *See supra* Part VII.B.2.

191. Miller, *supra* note 108, at 10,500.

192. *Id.*

193. *See id.*

194. *Id.*

195. *Id.* at 10,488 (citing Brooks, *supra* note 55); Grais & Boike, *supra* note 122, at 7.

196. Miller, *supra* note 108, at 10,501.

tenants "to make changes they would not otherwise make."[197] Every green lease should anticipate this future risk by ensuring contract language exists to allocate the cost and responsibility of any changes that may arise.[198]

VIII. CONCLUSION

Despite the troubling economy and the less-than-stellar commercial real estate market, opportunities exist for business-savvy building owners willing to invest in green construction. Market trends and environment-friendly regulations continue to increase the demand for sustainable real estate. Landlords and tenants wise enough to embrace the green movement will likely reap financial benefits from their investment, but under current contracting practices, these wise parties subject themselves to unwise risk. For pioneers in the industry, the only law available to protect landlords and tenants is the law of contract. A comprehensive green lease ensures each party's satisfaction as they embark on the ever-changing process of sustainability.

While the net lease rules the day, a hybrid lease, arguably a gross lease mingled with tenant-incentives, is the ideal solution for effective green leases.[199] It "transfers the fiscal responsibility for controlling operating costs back to landlords, who are far more qualified to do so than the tenants," and "[i]t creates a financial incentive for landlords to effectively design, build and manage high-performance sustainable buildings."[200]

In the end, the perfect green lease is an experiment in contract. To take the unique goals of two distinct parties and merge them into a third, even larger set of movement-driven sustainability goals is not an easy task for any lawyer. It is, however, a necessary and rewarding task that no other professional can perform.

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197. Grais & Boike, *supra* note 122, at 7.

198. *See id.*

199. *See* Friedenberg, *supra* note 109, at 1.

200. Whitson, *supra* note 48, at 18.

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