Environmental Upgrade Agreements.

Accelerating energy efficiency in commercial buildings.

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Content Overview:

- **Disclaimer**
- **Key Points**
  - Summary of EUAs
- **EUAs: Eligible works**
  - What can be done and how
- **Location and history**
  - Where they work and a brief history
- **Why EUAs work**
  - A comparison to traditional debt
- **The EUA process**
  - The process, timeline, and considerations
- **Case Study**
  - Sydney CBD Environmental Upgrade Agreement
- **Questions**
- **Important notice**
Environmental Upgrade Agreements: Key Points

- 100% funding for environmental upgrades repaid via the council rates mechanism

At the same time as the provision of first funding to the Building Owner, a series of environmental upgrade charges (EUCs) are declared by the Council.
Environmental Upgrade Agreements: Eligible Works

- The works must result in an environmental improvement to the use and occupation of the building
- Environmental improvements cut across energy, water, waste and sustainability
- An AS/NZS 3598-2000 Level 2 Energy Audit is required

- Base Building examples:
  - Boilers
  - Chillers
  - BMS
  - Windows and cladding
  - Lighting
  - Lift motors
  - Water recycling

- Tenancy examples:
  - Lighting
  - Kitchen boilers

Photo source: NAB
Environmental Upgrade Agreements: Common vs. Custom improvements

There are two types of improvements that can receive funding:

1. **Common improvements**
   - These are improvements with a proven record of producing either energy or water savings, or renewable energy, and therefore qualify as a pre-approved improvement.
   - Any common improvement included in an application does not need to undergo additional review or approval by Sustainable Melbourne Fund for eligibility.

2. **Custom improvements**
   - Any improvement not on the Common Improvements list.
   - Custom improvements require a business case and are assessed by a technical reference panel. Business case should cover:
     - A brief explanation of why the improvement meets the program's definition of an environmental upgrade
     - Any information, reports or case studies that support the explanation
     - A simple cash flow model showing the effect of the cost savings of the custom improvement
     - A list of examples of custom improvements is available from the Sustainable Melbourne Fund website.
Where EUAs work

- City of Melbourne
- City of Sydney
- City of Lake Macquarie
- North Sydney Council
- Parramatta City Council
- City of Newcastle

South Australia will legislate this year, and cities of Brisbane and Perth have active working groups. Victorian Government currently considering allowing EUAs state-wide as part of Plan Melbourne review.
Environmental Upgrade Agreements: A brief history

- **NSW Legislation**: 18/2/2011
- **First EUA: 460 Collins St**: 13/10/2011
- **EUA at 123 Queen St**: 20/12/2011
- **EUA at 470 Collins St**: 10/6/2012
- **EUA at 10 Valentine**: 1/12/2012
- **EUA at 501 Swanston St**: 24/10/2013
- **EUA at Sydney CBD building**: 25/11/2013

- **Sydney Parramatta**
- **Lake Maq**
- **North Sydney**
- **Newcastle**

- South Australia comments on draft legislation
- Victoria begins consulting for state wide EUAs
Why EUAs work: Advantage to traditional debt

<table>
<thead>
<tr>
<th></th>
<th>EUA</th>
<th>Debt</th>
</tr>
</thead>
<tbody>
<tr>
<td>No Security</td>
<td>✔</td>
<td>✗</td>
</tr>
<tr>
<td>No Financial Covenants</td>
<td>✔</td>
<td>✗</td>
</tr>
<tr>
<td>No financial reporting</td>
<td>✔</td>
<td>✗</td>
</tr>
<tr>
<td>No re-financing risk</td>
<td>✔</td>
<td>✗</td>
</tr>
<tr>
<td>(long tenor &amp; fully</td>
<td>✔</td>
<td>✗</td>
</tr>
<tr>
<td>amortising)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Non-recourse by financier to the building owner</td>
<td>✔</td>
<td>✗</td>
</tr>
<tr>
<td>Transparent tenant engagement</td>
<td>✔</td>
<td>✗</td>
</tr>
<tr>
<td>Pass through to tenant can improve financial performance</td>
<td>✔</td>
<td>✗</td>
</tr>
</tbody>
</table>
## Process Overview: Only two additional steps for an EUA

<table>
<thead>
<tr>
<th>Step 1</th>
<th>Building owner (B/O) conducts a level 2 audit to establish works and power savings.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Step 2</td>
<td>Building Owner completes and submits EUA application to local council. EUA template issued.</td>
</tr>
<tr>
<td>Step 3</td>
<td>Financier completes an abbreviated credit process.</td>
</tr>
<tr>
<td>Step 4</td>
<td>Financier issues draft Letter of Offer (10 page template); B/O and Financier then agree Letter of Offer (LoO).</td>
</tr>
</tbody>
</table>
| Step 5 | B/O, Council, Financier agree EUA.  
40 page template - not designed to be amended; Annexures are customised. |
| Step 6 | CPs need to be satisfied:  
Know Your Customer, verification forms/evidence,  
signed purchase agreements/construction contracts, etc. |
| Step 7 | B/O finalises work scope and signs purchase/construction agreements, as well as LoO and EUA. |
| Step 8 | Monies advanced based on contract terms. |
| Step 9 | Monies repaid each quarter from first Council date after works completed. |
Process Flow: The timeline for EUAs in Melbourne

1. Submitted application form to Sustainable Melbourne Fund
2. Financier commences credit assessment
3. SMF approval, start 28 day statutory waiting period
4. Letter of Offer signed
5. EUA signed

First drawdown
Considerations when planning for an EUA

- Common or custom improvement path?

- What are the projected savings?
  - Important to prove the business case
  - Both SMF and NAB need projections for our assessments
  - Don’t forget the maintenance savings

- Is there an opportunity for tenancy side improvements?

- Who will be providing the QS reports?

- When am I likely to need the funds?
  - Drawdown schedule needs to be set in advance and aligned to council rate periods
  - For smaller EUAs only one drawdown
Case Study: Sydney CBD Environmental Upgrade Agreement

- The EUA included a raft of retrofit works to lift the star rating of the building from 2 to 4 NABERS Energy Rating to attract quality tenants

Scope of Works

- Replacing:
  - tenancy light fittings and lights,
  - three lift motors
  - water pumps
  - Metering
  - Chiller and Boiler Replacement
- led to energy and maintenance savings for the tenants
- without capital expenditure by the tenants and no lease negotiating

EUA Agreement

- EUA appropriately shares and regulates the costs and benefits of the upgrade

Source: Sustainable Melbourne Fund
Case Study: Sydney CBD Environmental Upgrade Agreement

- The EUA included a raft of retrofit works to lift the star rating of the building from 2 to 4 NABERS Energy Rating to attract quality tenants

### Key Takeaways

<table>
<thead>
<tr>
<th>Building Owner</th>
<th>Tenants</th>
</tr>
</thead>
<tbody>
<tr>
<td>✓ Cash flow benefit</td>
<td>✓ Cash flow benefit without capital expenditure</td>
</tr>
<tr>
<td>✓ Competitive cost and diversified source of capital</td>
<td>✓ Improved tenancy space without rent review initiation</td>
</tr>
<tr>
<td>✓ Bundled purpose financing which matches payback</td>
<td>✓ Transparency in benefit sharing</td>
</tr>
<tr>
<td>✓ Tenant engagement + retention</td>
<td>✓ Better occupancy space</td>
</tr>
</tbody>
</table>

### Key Transaction Details

<table>
<thead>
<tr>
<th>Date of signing</th>
<th>Late 2013</th>
</tr>
</thead>
<tbody>
<tr>
<td>Building Owner</td>
<td>Undisclosed</td>
</tr>
<tr>
<td>Total Area</td>
<td>c.6,000m²</td>
</tr>
<tr>
<td>Number of Tenants</td>
<td>21, net leased</td>
</tr>
<tr>
<td>WALE</td>
<td>c.3 years</td>
</tr>
<tr>
<td>Capital Cost</td>
<td>c.$2,200,000</td>
</tr>
<tr>
<td>EUA Term</td>
<td>10 years</td>
</tr>
<tr>
<td>Est. Electricity Savings</td>
<td>c.$141,600 p.a.</td>
</tr>
</tbody>
</table>
Case Study: Sydney CBD Environmental Upgrade Agreement

- Drawdowns from Oct 2013 over a 12 month period
- C.$2.2m EUA fully amortised over 10 years

Cash flow benefit for owner:
- Quarterly capital recovery of c.$40k
- Cost/tenor of funds advantage
- Tax benefits of ownership

Cash flow benefit for tenant:
- Estimated tenancy energy and maintenance savings of c.$5k net of EUC contribution per quarter
- Savings increase over time

From 2014, an EUC of c.$70k per quarter for 10 years

Tenants under net leases pay c.$40k to Owner as contribution to EUC

Tenant saves c.$40k in energy and c.$5k from maintenance costs per quarter

Repayment of c.$70k per quarter for 10 years
Questions?

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