

**ITEM 2. REVISED ENVIRONMENTAL UPGRADE AGREEMENTS POLICY – ADOPTION****FILE NO: S101635****SUMMARY**

Environmental Upgrade Agreements are voluntary agreements between a building owner, a finance provider and a local council within NSW, which are designed to help overcome barriers to the implementation of environmental upgrades and retrofits to existing buildings.

Under an Environmental Upgrade Agreement, a finance provider advances funds to a building owner to undertake environmental works to an existing building. These funds are repaid by means of a charge on the relevant land, which is levied and collected by the relevant council as Environmental Upgrade Charges.

The NSW Office of Environment and Heritage, as managers of the Environmental Upgrade Agreements Program, developed a standard template contract that must be used by the three parties entering into an Environmental Upgrade Agreement.

Since the City resolved to enter into Environmental Upgrade Agreements in September 2011, it has entered into four such agreements, with total funds advanced of \$30.4 million.

Responding to industry feedback, the NSW Office of Environment and Heritage has sought to address issues to increase the number of Environmental Upgrade Agreements entered into through the revision of the template contract. The City provided extensive feedback to the NSW Office of Environment and Heritage throughout the template contract revision process.

The City's Environmental Upgrade Agreements Policy specifies the circumstances under which the City will enter into and administer an Environmental Upgrade Agreement. The policy also provides for the management of risks to the City and third parties that have not been addressed in the template contract.

The majority of the risks to the City that were dealt with in the previous policy have now been incorporated into the revised template contract.

The City's Environmental Upgrade Agreements Policy has been updated to reflect the amendments to the revised template contract. The City has consulted with key stakeholders on the updated policy.

The City is obliged to use the revised template contract on all new Environmental Upgrade Agreements. To ensure adequate protection of risks for the Council, no new Environmental Upgrade Agreements should be entered into until the revised Environmental Upgrade Agreements Policy is adopted.

**RECOMMENDATION**

It is resolved that Council adopt the revised City of Sydney Environmental Upgrade Agreements Policy, as shown at Attachment A to the subject report.

**ATTACHMENTS**

**Attachment A:** Revised City of Sydney Environmental Upgrade Agreements Policy

**BACKGROUND**

1. On 18 February 2011, amendments took effect to the Local Government Act 1993 to establish a legislative framework that provided for and authorised councils to enter into Environmental Upgrade Agreements. On 19 September 2011, Council resolved to enter into Environmental Upgrade Agreements in the City of Sydney Local Government Area (LGA).
2. An Environmental Upgrade Agreement is a voluntary agreement between a building owner, a finance provider and a local council within NSW where:
  - (a) a building owner agrees to carry out environmental upgrade works to a building (for instance works to improve the energy, water or waste efficiency of the building);
  - (b) a finance provider agrees to advance funds to the building owner to finance those environmental upgrade works; and
  - (c) the advance is repaid by means of a charge on the relevant land that is levied and collected by the council as Environmental Upgrade Charges, and then it is paid back to the finance provider.
3. The City's role is to levy an Environmental Upgrade Charge, as with other council rates and charges, which will then be payable through the rates system at dates and times as specified in the Environmental Upgrade Agreement.
4. The Environmental Upgrade Agreement mechanism is intended to address two key barriers that building owners face when considering environmental upgrades and retrofits to existing buildings:
  - (a) the "split incentive" issue, where a building owner pays for an environmental upgrade but it is the tenant that benefits financially (for example from lower electricity bills). This issue is reduced by allowing the building owner to pass on a proportion of the cost of the upgrade to their tenants, via the lease outgoings, as long as the tenant is no worse off; and
  - (b) the provision of competitively priced capital with long-term repayment schedules. With the capacity for a financial provider to secure the funds advanced under an Environmental Upgrade Agreement by having the charge levied as a debt against the land, financial providers should be able to offer competitive interest rates and longer term repayment schedules that reflect the time frame over which cost savings arising from an environmental upgrade can accrue.
5. Since 2011, market uptake of Environmental Upgrade Agreements has resulted in six agreements signed in New South Wales, four of which were signed by the City of Sydney.
6. Industry engagement undertaken by the NSW Office of Environment and Heritage identified a number barriers effecting take up in the market, including problems with the existing template contract document. It was proposed that a revision of the template contract should be undertaken.

**Environmental Upgrade Agreement Template Contract revision process**

7. The NSW Office of Environment and Heritage led the revision of the template contract commencing October 2015 to address the issues identified by industry and government stakeholders, including the City. These issues included legal corrections, simplification of language, notifications, protections and improving processes for the contract parties.
8. As a key stakeholder in the revision process, the City formed a working group including City Legal, Finance and Sustainability which provided extensive feedback to the NSW Office of Environment and Heritage, specifically that:
  - (a) the template contract be simplified and legally correct;
  - (b) all risks to council and other Environmental Upgrade Agreement parties, as previously identified by the City and managed via its policy, be added to the contract documentation;
  - (c) the City's internal processing and administration systems related to entering and administering Environmental Upgrade Agreements be considered and not negatively impacted;
  - (d) changes proposed by other stakeholders would not create new risks or additional administrative burden for the City; and
  - (e) a suitable mechanism be adopted to ensure appropriate transparency of Environmental Upgrade Agreements on land that would protect prospective purchasers and financiers. Over the coming months, options will be explored between the NSW Office of Environment and Heritage, NSW Planning and the City to deal with this matter. In the interim, the City will maintain a requirement for Environmental Upgrade Agreements exceeding \$5 million to be registered on title.
9. The NSW Office of Environment and Heritage incorporated all the key items requested by the City through the revision process.
10. The revised template contract has now been completed and endorsed by the Director General of the NSW Office of Environment and Heritage.

**Summary of key Template Contract changes**

11. The template contract contains the mandatory provisions to be complied with by each party and also includes a standard set of additional conditions that can be selected and included in the contract.
12. Key changes to the template contract are as follows:
  - (a) a restructuring of the document to provide a more streamlined contract;

- (b) the insertion of the majority of the City's previous policy items into the additional conditions and mandatory provisions including:
    - (i) notification to an existing financier of owner's intent to enter into an Environmental Upgrade Agreement;
    - (ii) notification to a prospective purchaser and financier of the existence of an Environmental Upgrade Agreement;
    - (iii) Council consent required for subdivision;
    - (iv) building owner's consent to the lodgement of a caveat if requested by council to provide transparency that an Environmental Upgrade Agreement exists on land, in order to protect prospective purchasers and financiers;
    - (v) the use of the City's payment dates and methods;
    - (vi) the requirement that the financial provider undertake a satisfactory credit assessment of the building owner;
    - (vii) the requirement to use a suitably qualified professional to carry out all calculations and reports on the environmental and cost savings from the Environmental Upgrade Agreement works; and
    - (viii) the mandatory use of direct debit for payments to council in keeping with the City's existing rates collection procedures;
  - (c) the requirement for the building owner to notify, as opposed to seeking consent from council, if they intend to sell the building;
  - (d) the requirement that a building owner will undertake an annual reconciliation of estimated and actual cost savings, and reimburse any overpayment by tenants contributing to an Environmental Upgrade Agreement;
  - (e) the removal of financial representations and warranties related to the loan provision not relevant to the template contract. These will be contained in the financier debt documentation thus removing significant duplication; and
  - (f) the removal for council consent to leasing changes, provided that all leasing changes are registered on title. This is required as a mandatory provision in the contract.
13. Changes to the template contract have been assessed by City Legal, Finance and Sustainability as having no impact on Council administrative processes, existing Council protections or enforcement procedure.

#### **Amendments to the City's Environmental Upgrade Agreements Policy**

14. Responding to changes made in the revised template contract, the Environmental Upgrade Agreements Policy has been reviewed and amended accordingly, in consultation with City Legal, Finance and Sustainability. The changes include:
- (a) developing a better document structure;

- (b) the removal of items now provided for in the revised template contract;
- (c) the simplification of wording surrounding council consent conditions related to the subdivision of land subject to an Environmental Upgrade Agreement; and
- (d) the addition of the following two minor process related items:
  - (i) all authorisations required to undertake building upgrades must be held by the building owner prior to making an application for an Environmental Upgrade Agreement; and
  - (ii) building owners may make pre-payments of an Environmental Upgrade Charge outside of the scheduled quarterly instalments. The City will only accept such a pre-payment where it is equal to or greater than the value of one charge payment as set out in the repayment schedule of the contract.

## KEY IMPLICATIONS

### Strategic Alignment - Sustainable Sydney 2030

15. The Environmental Upgrade Agreement program is aligned with *Sustainable Sydney 2030* strategic direction 2, which provides a road map for the City to become A Leading Environmental Performer. Retrofitting buildings to improve their environmental performance will be essential to achieve this goal and Environmental Upgrade Agreements should help to facilitate this.

### Organisational Impact

16. The revised template contract and policy will have no impact on the City's administration of Environmental Upgrade Agreements nor produce any additional risks to the City.

### Environmental

17. The introduction of Environmental Upgrade Agreements by the City was intended to accelerate action by building owners to improve the environmental performance of the city's existing building stock. It is expected that the amended template contract and revised policy will allow greater uptake of Environmental Upgrade Agreements, thereby further contributing to the achievement of *Sustainable Sydney 2030* targets.

## BUDGET IMPLICATIONS

18. Nil.

## RELEVANT LEGISLATION

19. Local Government Act 1993, Part 2A Environmental Upgrade Agreements.
20. Local Government (General) Regulation 2005.
21. Guidelines for Environmental Upgrade Agreements as published in the Government Gazette of NSW dated 18 February 2011.

**PUBLIC CONSULTATION**

22. The City presented the revised Environmental Upgrade Agreements Policy to the key stakeholders, including the NSW Office of Environment and Heritage, Property Council of Australia and Eureka Funds Management. No issues or concerns were identified by any party.

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