



Tom Marshall
Partner, Gerald Eve
Tel. +44 (0)20 3486 3702
tmarshall@geraldeve.com



Edward Green
Associate, Gerald Eve
Tel. +44 (0)20 7518 7253
egreen@geraldeve.com



Andrew Cooper
Director, EVORA EDGE
Tel. +44 (0)1252 268368
acooper@evoraedge.com



Paul Henson
Partner, Irwin Mitchell
Tel. +44 (0)20 7421 3944
paul.henson@irwinmitchell.com

ENERGY PERFORMANCE IN NON-DOMESTIC BUILDINGS

Owners and occupiers of non-domestic buildings are seeking to understand in greater detail how energy is being used in buildings and how energy consumption may be reduced in line with net zero carbon commitments and science-based targets. Whilst Energy Performance Certificates (EPC) ¹ are seen by many as an imperfect tool, the future trajectory of Minimum Energy Efficiency Standards (MEES), increasing from an EPC E in 2023 to an EPC B by 2030, emphasises the importance of EPCs.

This short briefing note, prepared with EVORA EDGE and Irwin Mitchell, provides an insight into complying with MEES and reducing energy consumption and carbon emissions in non-domestic buildings. It also points towards alternative approaches to improving energy performance in non-domestic buildings which the government has recently consulted on. It will be relevant to investors, developers, owners and occupiers of commercial buildings.

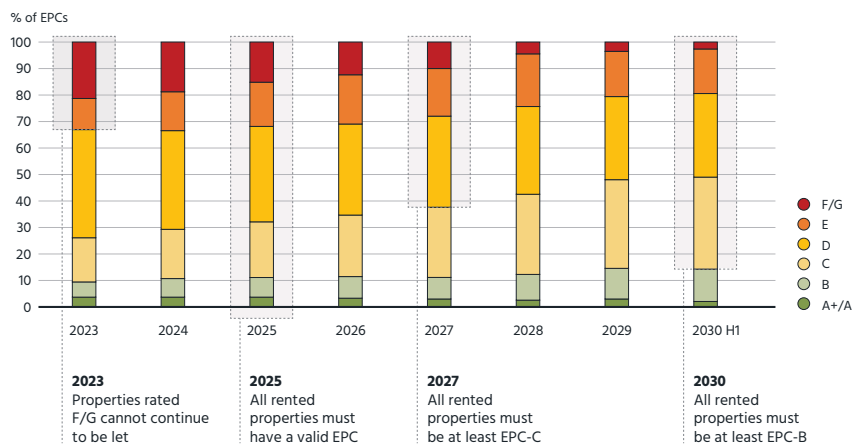
How big is the challenge of MEES?

Of the c.91,000 non-domestic EPCs lodged in 2019, only 15% were A+/A or B rated. If we look back further, the data is even more stark. Over the last 10 years, it is estimated that less than 12% of all EPCs lodged were B or higher. This means that the **vast majority (88%)** of non-domestic properties will need to be improved over the next 10 years (during the life of the EPC) to comply with potential future MEES requirements. In real numbers, this equates to over **half a million individual assets** that would need to be improved, representing a real challenge for the property industry.

Figure 1. EPC data and proposed compliance windows to 2030 for non-domestic buildings

EPCs expiring, non-domestic properties

Source: Gerald Eve



Minimum Energy Efficiency Standards (MEES)

The *Energy Efficiency (Private Rented Property) (England and Wales) Regulations 2015* are designed to tackle the very least energy efficient properties in England and Wales – those rated F or G on their Energy Performance Certificate (EPC)². The minimum level of energy efficiency provisions, mean that, subject to certain requirements and exemptions:

- a) Landlords of non-domestic private rented properties (including public sector landlords) may not grant a tenancy to new or existing tenants if their property has an EPC rating of band F or G.
- b) From 1 April 2023, landlords must not continue letting a non-domestic property which is already let if that property has an EPC rating of band F or G.

The Government confirmed in the Energy White Paper (2020) that the future trajectory for the non-domestic MEES will be EPC B by 2030.

A variety of case studies are appended to this briefing note to illustrate EPC requirements, ten year validity and the Minimum Energy Efficiency Standards (MEES).

The fines for non-compliance range from £5,000 to £150,000. Temporary, five-year exceptions and exemptions, include:

- **High cost** i.e. works that would exceed a simple seven year payback
- **Impact on value** i.e. works that would decrease the capital value of the property by more than 5%
- **Unsuitable measures** i.e. works that would have a negative impact on the fabric and structure of the property, or building of which it forms part
- **Consent** i.e. works which require consent, but that consent is not forthcoming
- **New position** i.e. a new landlord may be exempt from meeting the minimum standard for six months

All exemptions must be lodged with the PRS Exemptions Register, and must include related evidence. Exemptions are non-transferable – a building sold cannot rely on a previous owner’s exemption. Exemptions expire after five years (except in the case of exemption 5, which expires after six months), and once expired, a landlord will need to again try to reach

the standard if they wish to let the property, or register another valid exemption.

At present, MEES would not apply to a building which does not have an EPC or where an EPC has expired. Unless a building is let or sold there is currently no trigger for an EPC to be produced.

If there is any doubt about whether a property (or the building it is in) is legally required to have an EPC (or whether an EPC was legally required or voluntary), expert advice should be sought.

What changes should we expect in the future?

The Government recently consulted on two important proposals on energy performance and a response is expected in the autumn.

Surprisingly, the consultations proposed two slightly different approaches going forward, one which promotes a regulatory framework based on the EPC (MEES) and one which would establish a performance-based policy framework for larger commercial and industrial buildings over 1,000 sq m (perhaps using the NABERS UK scheme, which has recently been introduced on a voluntary basis). A summary of the consultations is appended.

In 2021 a range of changes to how EPCs are calculated is expected, including an update to the SAP emission factors as well as new minimum standards on ventilation, thermal efficiency and ventilation proposed in the Future Buildings Standard consultation. These changes could affect a building’s current EPC rating and it is possible that an existing EPC rating could worsen from this year or 2022 onwards, even if no changes are made to the building. For example, we already know that under the new SAP emission factors (SAP 10.1) the change in emissions from grid supplied electricity is significant so systems that use fossil fuels, such as gas could be heavily penalised.

The changing of legislation is likely to only heighten existing concerns regarding MEES for both landlords and lenders in relation to marketability, rental value, capital values and security of income. This may also impact the lending system as properties with lower ratings will have greater levels of risk applied to them. As lease lengths continue to shorten and companies are looking to improve their Environmental, Social, and Corporate Governance credentials, the impact of the MEES legislation is likely to become more of an issue and therefore of more importance across all commercial property sectors.

¹ An EPC is a certificate which summarises the energy efficiency of a building. It usually lasts for 10 years, with certain exceptions.

Considerations and approaches to mitigating and managing risk and improving energy performance.

It is important to remember that EPCs are purely a compliance tool and are not a robust indicator of an energy efficient building. They will not, operationally speaking, deliver net zero carbon buildings. However, EPCs could or should be a by-product of the approach to managing a building.

When considering the future trajectory of MEES, it is important to work backwards to ensure the risk of MEES is also factored into the plan for a building.

In making any investment in energy performance, the most important element to understand is how much of those costs may be reclaimed back under the service charge and how much will need to be capital expenditure.

The best way of doing this is through the planned maintenance report (PMR) which will identify the life-cycle costs of existing equipment.

It is impossible to quantify the likely costs of improving a building's poor EPC without a model as every building is different.

We would recommend the following approach moving forward:

Table 1: Proposed tasks for managing MEES compliance and energy performance

Item	Task	Purpose
1	Obtain the current EPC model (not just certificate) and validate its result.	To accurately assess the level of risk under existing and/or proposed MEES and EPC methodologies.
2	Convert the existing model to DSM or build a new model in DSM. Only use SBEM where the consultant provides a reason as to why DSM is not appropriate, and never use SBEM for anything regarded as investment grade and/or with a 5+ year holding strategy.	A DSM model cannot only produce an EPC certificate but also identify the changes required in the building to achieve a 'B' rating and a net-zero pathway by 2050. It can also be adapted to support with NABERS UK ratings if required in the future.
3	Use the model to identify a pathway to ensure compliance with MEES or Net Zero Carbon (NZC) targets.	It is not possible to prepare a MEES strategy without an EPC model, and these models can be adapted for more sophisticated NZC (or NABERS UK) purposes.
4	Use the planned maintenance report (PMR) to calculate lifecycle costs. These can include cost plans to maintain and replace or to change and improve.	This would help identify which costs can be recovered under the service charges and which changes would need capital outlay and the date that outlay would be required.
5	Update the model whenever Category A, A+ or B work is undertaken to ensure the information in the model is always accurate.	This ensures the model can be used as a decision-making tool at any time and EPCs can be produced whenever required without the cost of rebuilding the model each time.

Notes on table:

- This table has been prepared by EVORA EDGE
- A PMR is a 5/10 life cycle cost report.
- There are two types of software used to generate EPCs – SBEM (simplified building energy model) and DSM (dynamic simulation model). An SBEM model is built purely for the purposes of producing an EPC. A DSM is a model with far greater levels of detail and accuracy. Whilst it can generate an EPC it can also be used for a wide range of asset management purposes such as BREEAM calculations, climate change modelling and productivity metrics.
- Our advice is based on what we believe is the most efficient long-term management of an asset. However, it is not necessarily the cheapest method of obtaining a statutory EPC certificate and each case should be considered in own its own right. For example, a simple retail or industrial unit might suit a different – more cost-effective approach.

Note: Landlords will wish to be aware that the methodologies underpinning EPC calculations are updated periodically. This means that, depending on the characteristics of a particular building, or unit within a building, the EPC band may change irrespective of any improvement works undertaken. Therefore, even if an EPC for a property is current (i.e. less than ten years old), the landlord may wish to obtain advice as to the rating that would apply to the building if an EPC were commissioned, before deciding on a particular course of action in relation to minimum standards compliance.

APPENDIX A

EPC AND THE INTERACTION WITH MEES

If an EPC certificate has been registered, you can search the online government databases below:

PROPERTIES IN ENGLAND AND WALES

EPC Requirements, Ten Year Validity and the Minimum Energy Efficiency Standard

The following scenarios are provided as illustrative examples, highlighting the ten year validity of an EPC and the interactions with the minimum standards:

Scenario one

A landlord intends to let a property on a new lease:

If the property already has an EPC which is less than ten years old then this EPC can be used to let the property. If the EPC is more than ten years, or if there is no EPC, then the landlord will be required to obtain a new EPC to market and let the property. If that EPC shows an energy efficiency rating of F or G then the landlord will need to carry out sufficient energy efficiency improvement works to improve the property to a minimum of E (or register a valid exemption if applicable) before issuing a tenancy agreement.

Scenario two

A property let on a ten year lease with an F rated EPC obtained, as legally required, in 2015:

On 1 April 2023 the landlord is continuing to let the property and will have to comply with the minimum energy efficiency provisions because there is a valid EPC which the landlord was required to obtain (the EPC will continue to be valid until 2025).

Scenario three

A property let on a twenty year lease with an F rated EPC obtained in 2012:

On 1 April 2023 the landlord is continuing to let the property but in this scenario will not be captured by the minimum energy efficiency provisions because the EPC expired in 2022, and there is no legal requirement on the landlord to obtain a new one at that point (because the tenancy is ongoing). The landlord will only be required to obtain a new EPC (which will trigger a need to comply with the minimum energy efficiency provisions) if they intend to re-let the property (to the current tenant, or to a new tenant) once the current lease expires, or if they (of their tenant) modify the property in a manner which would require a new EPC.

Scenario four

Based on scenario three, if the tenant in 2025 wishes to sublet the property, the tenant (who will become a sub-landlord) will be required to obtain an EPC to market the property. If this EPC shows an F or a G rating then the landlord will need to comply with the minimum energy efficiency provisions because the property now has a valid, legally required, EPC.

APPENDIX B

THE NON-DOMESTIC PRIVATE RENTED SECTOR MINIMUM ENERGY EFFICIENCY STANDARDS: IMPLEMENTATION OF THE EPC B FUTURE TARGET

This consultation sought views on how to address matters regarding compliance and enforcement likely to occur with the proposed increase of the minimum standards of **C from 1 April 2027** (the interim milestone), to **B by 2030** and for improvements to be undertaken by landlords over the period up to 2030, rather than landlords implementing changes once the new legislation has been implemented.

A new implementation and enforcement framework based on ‘compliance windows’

First Compliance Window: EPC C (2025-2027)	Second Compliance Window: EPC B (2028-2030)
<ul style="list-style-type: none"> 1 April 2025: Landlords of all non-domestic rented buildings in scope of MEES must present a valid EPC. 1 April 2027: All non-domestic rented buildings must have improved the building to an EPC \geq C, or register a valid exemption. 	<ul style="list-style-type: none"> 1 April 2028: Landlords of all non-domestic rented buildings in scope of MEES must present a valid EPC. 1 April 2030: All non-domestic rented buildings must have improved the building to an EPC \geq B, or register a valid exemption.

At present, authorities responsible for enforcement do not have sufficient data readily available to identify breaches of MEES. The consultation is proposing that any increases to MEES will also require landlords to submit a valid EPC to a central register in order to be able to let their property. If the property is below the standard required, the landlord will have a two year “compliance window” from the date of submission to present a valid EPC for their let properties.

The Government also intends to address the current uncertainty regarding heritage buildings by clarifying that all let buildings, whether or not they are listed or in a conservation area, must have a valid EPC. Consideration is also being given to lettings of shell and core space.

The expectation is that it will be compulsory to renew EPCs and for EPCs to be updated once works have been completed. At present, once an EPC has expired after 10 years, a new and valid EPC is only required on a sale or when a new lease is granted. Current legislation only relates to landlords, but the proposals also include obligations on tenants and the impact of their fit out works. This is likely to impact a tenant’s ability to underlet or assign their lease in future.

APPENDIX C

INTRODUCING A PERFORMANCE-BASED POLICY FRAMEWORK IN LARGE COMMERCIAL AND INDUSTRIAL BUILDINGS IN ENGLAND AND WALES

This consultation sought views on the Government's proposals that owners and single tenants of buildings above 1,000 sq m will be required to obtain a rating for their building on an annual basis, and have that rating disclosed publicly online.

The Government is considering implementing a three-phase rating system starting with the office sector, as it considers this sector to be best placed in comparison to other non-domestic sectors.

The Government proposes that, for rented offices above 1,000 sq m, their obligations under Non-Domestic PRS MEES are addressed when they are onboarded onto the performance-based framework so that:

- The office's EPC will be reviewed when the building is onboarded onto the performance-based policy framework. If the building does not have an EPC, an EPC will be conducted as part of the onboarding process
- The cost-effective measures that the office would need to install to get up to an EPC B will be determined and agreed
- Once those measures are agreed, the building owner will have until 2030 to install those measures
- To demonstrate compliance, the building owner will only need to show that the agreed measures have been installed by 2030

Buildings under 1,000 sq m will remain solely in the Non-Domestic PRS MEES regulatory framework.

The proposals could see the NABERS UK scheme, brought over to the UK from Australia by the Better Buildings Partnership in November last year, form the basis for the performance-based policy framework.