INDUSTRY INSIGHT

BBP BETTER BUILDINGS PARTNERSHIP

2015 GRESB SURVEY CONSULTATION RESPONSE

NOVEMBER 2015

Introduction

The Better Buildings Partnership (BBP), a collaboration of the UK's leading commercial property owners who are working together to improve the sustainability of existing commercial building stock, welcomes the growing influence GRESB is having on the global commercial real estate sector and the increasing support from investors in its use as a benchmark for ESG best practice and performance.

Given the growing rate of participation, the BBP believes that GRESB has a significant opportunity to drive market transformation across the real estate sector at a global scale. The BBP provided its first consultation response in 2013 and welcomes many of the changes GRESB has implemented and the progress which has been made over the past 24 months, as well as the planned changes for future years. Specifically, following our 2014 Consultation Response, the BBP was pleased to see the following recommendations implemented into the 2015 Survey and Guidance:

- Developing a scoring methodology which reflects the split between Environmental, Social and Governance issues;
- Maintaining the way data points are requested between years;
- Confirming the approach which should be used for the sale and acquisition of assets;
- Providing greater transparency on the data validation and quality assurance processes;
- Providing clarification on the scoring methodology when 'not applicable' is selected.

And confirmation that the following points are being considered for the 2016 Survey, to which we therefore look forward to seeing how they will be incorporated:

- The principle of analysing information as a ratio to value rather than floor area which would be of more relevance to investors;
- How the principle of 'managed' and 'indirect' can be used more widely throughout the Survey; and
- Incorporating green building ratings into scoring beyond the simple existence of a certificate.

We also note that the Survey is evolving further to assess operational performance. The BBP has extensive experience in measuring and benchmarking operational performance of commercial property portfolios through our Real Estate Environmental Benchmark and acutely understands the complexities involved. We'd therefore be delighted to share our experience with GRESB to help your understanding on the advantages and disadvantages of different types of analysis and how performance can most fairly be assessed.

As the GRESB Survery evolves, we feel there are opportunities for continued development and improvement, both in terms of the value which it provides for its stakeholders, and its ease of use to participate by property companies and fund managers. In this light, BBP members who participate in the GRESB Survery have provided the following recommendations for GRESB's consideration as part of its 2015 consultation process which we hope are viewed in a positive and constructive light.

RECOMMENDATION 1

The GRESB Survey has a strong influence on how sustainability is addressed and implemented within the commercial real estate sector therefore it is critical that each question has an appropriate investment rationale behind it.

An overarching issue which the BBP believes must be addressed in order for GRESB to develop as a valuable tool for both property companies/funds and investors is that the investment rationale for a number of questions, both in terms of the value investors receive from their investor reports and how collecting and submitting data translates into performance and actions to improve performance encourages the correct behaviour from participants, should be reflected to a much greater extent. This would ensure both participants and investors are fully aware of the reasoning for asking each question and why it relates to the ESG performance of the property company/fund. This idea of 'investment rationale' i.e. the human and financial resources borne by property companies and real estate funds balanced against the benefit received by the companies/funds themselves and in turn their investors, should also be used as a guiding principle for the future evolution and refinement of the Survey. This principle should also be applied to the weighting of the questions within the Survey.

RATIONALE

The GRESB survey is now having a direct impact in the way in which ESG policies and strategies are being implemented for real estate investment. Whilst this is a welcome response from the market it also highlights the importance that in bringing about change, the Survey needs to ensure it is bringing about the right change. I.e. it is driving the behaviours from both investors and participants that truly results in improving the ESG performance of the commercial real estate sector. This can be achieved two-fold:

1. Asking questions that are directly aligned to investment rationale; and

2. Scoring performance in a way that encourages behaviours from participants that achieve the greatest improvements in ESG performance.

From a cost benefit perspective, any prudent investor should want to ensure that firstly, the Survey is providing the relevant information that is material to their investment decisions in terms of risk mitigation and demonstrating ESG performance in a transparent way; and secondly, the Survey is encouraging companies/funds to direct their resources towards driving performance improvements and gathering data in those areas accordingly.

However, in our view, this is currently not the case and feel that many of the questions asked and their associated weighting within the Survey are not completely aligned to investor value and materiality but more academic in nature.

When raising this issue in the past, GRESB have stated that they feel this issue is already taken into consideration with their Investor Committee who help shape and evolve the Survey and ensure questions are of relevance to investors. With this in mind, the BBP felt it would be helpful to highlight the following specific questions/areas where we feel the benefits of requesting and analysing such data are unclear for the Investor Committee to review:

- **How the Survey penalises certain asset types as a result of management control rather than ESG performance which in turn diverts attention to where greatest ESG improvements can be made:** for example, equally treating the provision of base building energy consumption data for managed assets as providing tenant data which is not purchased by the landlord. It is unclear what benefit investors receive by property companies/funds spending a significant amount of resources requesting tenant energy data for NNN/FRI leases or where the tenant procures their own energy supply and when the property company/fund has no control over the performance of that space and diverts efforts from focusing efforts in making improvements where the property company/fund can make the greatest ESG improvements. Please see Recommendation 2 and Recommendation 3 for further details and opportunities regarding this point.

- **How the Survey breaks down performance based on floor area rather than value:** many of the questions analyse performance based on a property company / fund's floor area. For example, the existence of green building certificates, energy ratings, building assessments, metering and energy/water efficiency measures. However, it is far more relevant from an investor's perspective, to understand ESG risk as a ratio of value rather than floor area. This would align with standard financial reporting and the more common way data and risks are analysed internally by participants. The Performance Indicators section, however, is one area where performance should remain as being normalised by floor area.

- **How the Survey poses a number of questions to which the participant answers yet does not contribute to the overall score:** for example, Question 30 assesses a property portfolio/fund's level of compliance in terms of mandatory energy ratings, as well as an overall performance score. For Energy Performance Certificates (EPCs) it requests that the participant calculates a weighted score. Providing this information is particularly resource intensive given the data collection and bespoke calculations required. However, no additional scoring is awarded to participants that go through this process. If not points are awarded it must be assumed that this is of no material interest to investors, and therefore no reason for it to be included in the Survey. Interestingly, whilst geographically specific, in the UK the EPC rating is one of the most important ESG indicators for any investor due to the significant risk posed by Minimum Energy Efficiency Standards.

- **How the Survey duplicates effort by asking questions that are standard in any new investment mandate:** for example, requesting information on I.T security, bribery and corruption policies. If these issues were of interest to investors, details would be requested and answered at the RFP stage and they therefore do not need to be repeated within the Survey.

RECOMMENDATION 2

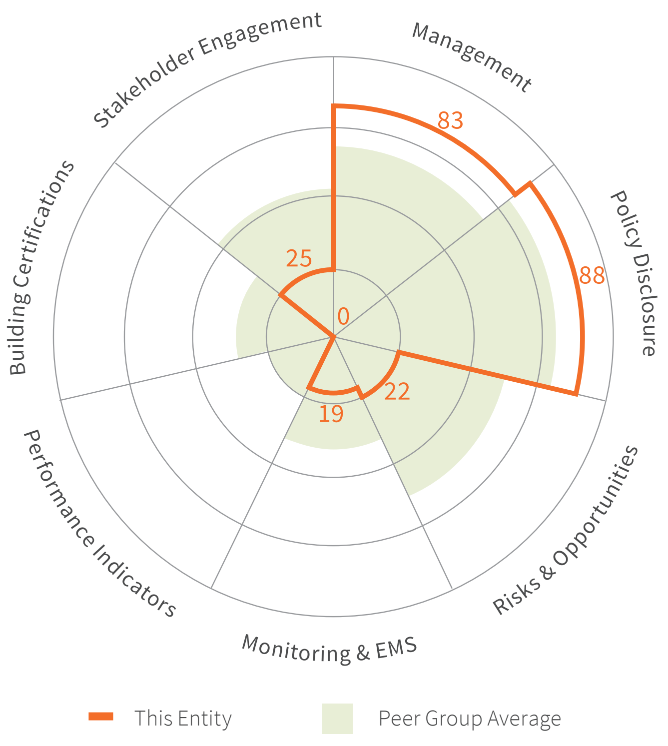
The principle of 'managed' and 'indirectly managed' assets should be integrated more widely throughout the Survey and used as a key differentiator to determine what questions participants should answer i.e. create separate questions for 'managed' assets and 'indirectly managed' assets.

RATIONALE

The Survey asks for information where the answers, and resulting performance, are significantly impacted by the degree of management control a participant has over the building i.e. whether it is an asset where the property company/fund procures some portion of the energy supply or a NNN/FRI lease (what is termed an 'indirectly managed' asset within the Survey) where the tenant is responsible for the procurement of energy supplies. In the UK, the average lease length is 6 years (and higher for some funds). For FRI/NNN assets the principle opportunities to make improvements is prior to letting during refurbishment. Once the unit is let, it is then the responsibility of the tenant to fit-out, maintain and improve the asset. Furthermore, tenants will often renew a lease which further extends the time before a participant may have an opportunity to make any improvements to the asset. Therefore assessing whether a FRI/NNN assets have implemented certain measures within a four year period (e.g. Question 16, 17 and 18); the level of the portfolio that is covered by an EMS, the data management processes in place; the way in which it monitors energy consumption (Questions 20, 21, 22 and 23); whether it collects energy, GHG, water and waste consumption (Questions 24, 25, 26, 27) is penalising this asset class purely on the nature of how that asset is leased and occupied.

This is highlighted in Figure 1 below which shows the GRESB scoring by dimension for one of our member FRI funds. The principle reason for the resulting low scores are not due to actual ESG performance of the property company/real estate fund, but as a result that for many questions an answer was not able to be provided as they were not applicable. This is particularly true for the Performance Indicators section where the landlord does not procure energy on behalf of the tenant and is therefore unable to submit data.

Figure 1. Example GRESB Survey scoring by dimension for BBP member FRI fund.



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We believe it would be more appropriate to have a scaled down, and therefore more comprehensive set of questions for 'indirectly managed' assets that measure a property company/fund's performance during refurbishment opportunities. This could easily be facilitated via the following:

- A separate and appropriately tailored set of questions for 'indirectly managed' assets in the same manor New Construction & Major Renovations is treated. The remaining set of questions to only apply to 'managed' assets; and
- The weighting of the Performance Indictor section to favour the performance 'managed' assets over 'indirectly managed' assets (See Recommendation 3).

Additionally, GRESB stated it would look to help address this issue by creating a peer group for 'NNN/FRI funds' if six or more such funds were submitted. This was not created for the 2015 results. However, given that our membership alone submitted five FRI funds we hope this will be included for 2016.

It is understood that GRESB is aware of this issue and we look forward to seeing how it will be addressed in future Survey iterations.

RECOMMENDATION 3

Provide clarification on how the level of a participant's management control affects the scoring methodology within the Performance Indicators section.

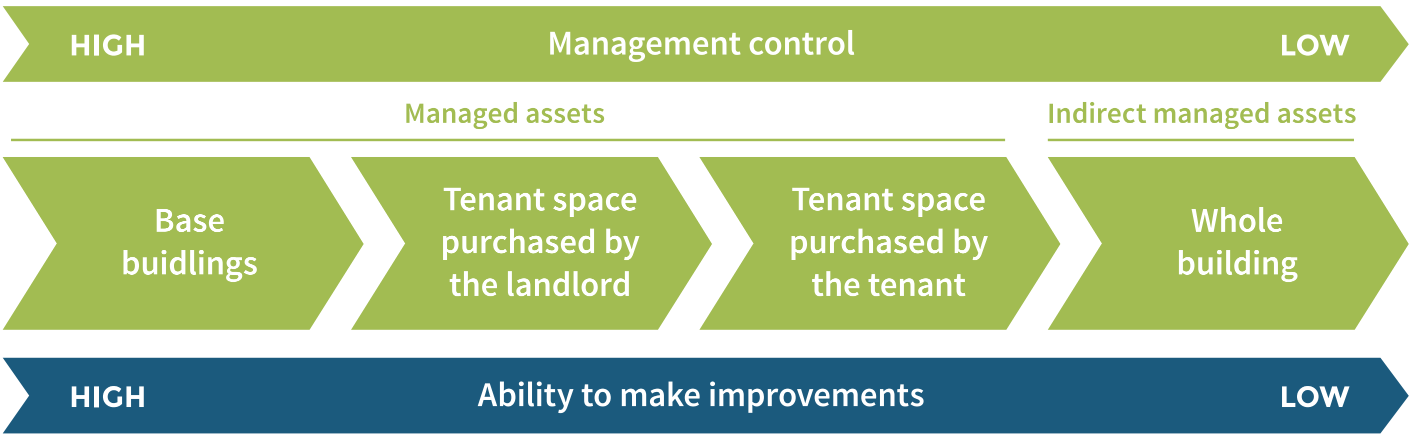
It is unclear whether there are different weightings given to the scoring of 'managed' and 'indirect' assets as well as the breakdown of 'base building', 'tenant space' or 'whole building' within 'managed' assets, based on the level of management control a property company/fund has.

RATIONALE

In general, and from experience within our members, significant efficiencies can be made in terms of the operational performance (energy, water, waste etc.) across all commercial properties. However, the ability for a commercial property owner to make such improvements is directly linked to the level of management control they have. As the level of management control reduces the level of difficulty to make improvements increases. Figure 2 provides a simple illustration of where commercial property owners have the greatest ability to make improvements to the properties they own and operate based on the Performance Indicator classifications the Survey uses.

We feel that through the implementation of carefully considered weightings, GRESB can encourage property companies/funds to place greater emphasis on making improvements where they have the greatest ability to do so i.e. rewarding companies for making energy reductions for base building managed assets over collecting tenant consumption data for indirectly managed assets. By incentivising participants to focus on the areas which will have the greatest impact on improving ESG performance, GRESB will be more effective in driving change across the global real estate market. However, this is currently not possible without the appropriate level of transparency in the scoring methodology.

Figure 2. Illustration of a commercial property owner's ability to make improvements in relation to management control.



RECOMMENDATION 4

Continue to develop the performance breakdown by each E, S and G category.

We welcome the move within the 2015 survey to highlight which category (E, S or G) each question relates to, and within the 2015 results provide individual scores by each category. This change will help investors to more easily understand and incorporate scoring results into their investment processes and allocation decisions, as well as dovetailing more closely with how ESG ratings are used across other investment asset classes.

RATIONALE

This approach fits more naturally with typical ESG categories for which investors are increasingly asking for details and helps all stakeholders better differentiate between the individual E, S and G categories. However, it is noted that the average 'E' score is lower than respective 'S' and 'G' categories. This is due to the fact the 'Implementation & Measurement' score of this category is not only based on the environmental policies and measures in place, but also the actual environmental performance of that property portfolio/fund. It is therefore important that investors and stakeholders understand the key differentiation within this category and how it impacts on scoring.

RECOMMENDATION 5

Provide details on how the GRESB Survey Green Star scoring will develop over time.

The results of the 2015 Survey show that a Green Star performance is now the average performance of the property companies/funds that participate. Whilst this is an encouraging sign is raises the question of how the Green Star scoring will develop over the coming years.

RATIONALE

As property companies/funds continue to drive improvements and their respective GRESB scores increase over time there is a risk that, in the coming years, all participants could reach the green star status. This would make it difficult for investors and stakeholders to identify high performers which in turn could devalue to the achievement. It would therefore be helpful to understand how GRESB intends to address this issue over time. For example:

- Make the Green Star threshold a relative one whereby it is moved each year depending on the average performance of the portfolio. e.g. only the highest scoring 25% of participants are awarded green star status.
- Keep the Green Star threshold fixed but break the categorisation down and create multiple Green Star categories to distinguish performance e.g. 1 Green Star up to 5 Green Stars.

It is interesting to note that GRESB has included a new overall metric – the 'GRESB Rating' providing a 1-5 score based on its quintile position relative to the global GRESB database. This new rating was well received by the BBP membership and it is therefore questioned whether this methodology will become the primary rating methodology overtime? Whatever the decision made, it is recommended that the GRESB Executive select and use one rating system rather than introduce new additional layers which will only increase confusion amongst stakeholders.

RECOMMENDATION 6

Amend the scoring methodology when 'not applicable' is the appropriate response to a Survey question so that the participant is not unfairly penalised.

Currently, when a participant selects 'not applicable' for any given question the answer is scored as zero. It is recommend that the methodology is adapted so that the denominator (total points available in the Survey) to which a score is marked against is adjusted accordingly when 'not applicable' is selected.

RATIONALE

Currently, participants are unfairly penalised simply because the questions are not applicable to their property portfolio/fund. This is particularly true for FRI

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properties/funds as highlighted in Recommendation 2. Unless investors are unaware of this potential issue for any fund they are assessing they may incorrectly believe that the specific property company or fund is performing poorly in comparison to its competitors. Providing a system whereby the total points available is adjusted by removing the points attributed to those questions that are not applicable would allow property companies and real estate funds to be compared on more equal terms.

RECOMMENDATION 7

Remove the time frame restriction when asking whether energy and water efficiency measures have been installed across the portfolio.

RATIONALE

In our 2014 Consultation Response we queried why Questions 17 and 18 ask for information regarding the types of energy and water efficiency measure that have been installed across a property company/fund's portfolio for a specified three year period; and argued it would make more sense for this time frame to be removed as it automatically excluded properties where measures may have already been installed more than three years in advance of completing the Survey.

The time frame for the 2015 Survey was extended to four years and it is therefore questioned whether the 2016 Survey will again extend this to five years? The rationale for the specific timeframe also remains unclear as, for example, it does not appear to align with warranty periods or average lease lengths. Commercial property owners do not generally collect information on the timeframes at which energy and water efficiency measures were installed. At most, simply whether they exist or not. This is especially true for companies where churns within their portfolio are high and new properties entering the portfolio are unlikely to have information on installation dates of efficiency measures readily available, or for new build where there will be no need to install additional measures during the specified timeframe.

Additionally, from both an ESG performance and an investors' perspective what is important is that such measures exist within the property portfolios they invest in rather than that which has been installed over the past four years. We therefore recommend that the time frame is removed and the questions simplified as to whether such measures exist across a property portfolio.

This is also an additional example of questions that should only be applicable to 'Managed Assets'. Firstly, it is very challenging for a property company/fund to know what efficiency measures a tenant has installed in an FRI property and therefore to report that information. Secondly, if in the instance a tenant invests in efficiency measures at a property with an FRI lease and provides that information for the landlord to report to GRESB, it is questionable whether the landlord should even receive the benefit of additional scoring in the Survey unless they are directly involved in the process e.g. supporting audits or funding.

RECOMMENDATION 8

Consider changing the term 'indirect' to 'no management control'.

RATIONALE

As mentioned in our 2014 Consultation response, GRESB define 'indirect' properties as those where property companies/funds do not have management control. However, this is not the common use of the term within the real estate industry, which may lead to confusion for participants. For the real estate community, 'indirect' assets are those where a property company/fund has an indirect relationship with the property i.e. investing in another product that directly invests in property such as buying shares in a publically listed property company or investing in real estate fund. The term 'no management control' would be far clearer. We appreciate GRESB operations at an international level, however, this confusion around the terminology was still an issue for our members in 2015, many of whom have global real estate portfolios.

RECOMMENDATION 9

When changes to the Survey questions are made whilst the Survey is open, all participants should be informed of changes effectively.

RATIONALE

We welcome the fact that changes can be made whilst the Survey is open to correct errors in the Survey questions. This occurred during the 2015 Survey when changes were made to how estimations were treated and clarifications made on how outdoor/external energy consumption data should be provided. However, not all participates received an email notifying them of the changes with communications only circulated to key contacts rather than all those involved in collating and providing data. A process should be implemented so that all contacts are notified of any changes to the Survey whilst the Survey is open. It is suggested that rather than updating the Survey Guidance mid-survey and assuming people will be aware of any changes, the Survey Guidance is kept fixed at the point of the Survey opening and an FAQ page is created on the website which provides details of updates and clarifications. This could be updated regularly and participants could then see whether any changes had been made since their last check.

RECOMMENDATION 10

Provide greater transparency on the data validation and quality assurance processes.

RATIONALE

An open and transparent data validation process is crucial for GRESB to remain a benchmark of quality and credibility that the industry can trust. It is welcome to see that in 2014 every form of data validation increased in number, however it is important that such a process is used to identify any errors in submissions. Specifically in relation to on-site visits, two of our members received on-site inspections, yet were not required to provide evidence throughout the day visit and the purpose appeared more of a feedback session rather than an audit. It is felt that on-site visits could be used more effectively for the GRESB team to request evidence from participants and understand how participants are interpreting and answering specific questions.

Additionally, it is understood that the auditing and quality assurance process is conducted at random by GRESB, however, it is recommended that a stratified sampling method is used to ensure a variety of differing performers are selected. In addition this would provide the opportunity to weight sampling towards the highest achievers e.g. to verify the performance of those that are awarded 'sector leader' or those that sit in the highest quintile of the GRESB Rating to ensure credibility.

RECOMMENDATION 11

Provide greater transparency on the scoring of qualitative questions.

RATIONALE

A number of questions within the Survey request qualitative information to be provided which is then scored e.g. Question 1.1 – Does the entity have a specific sustainability objective? [If so,] Communicate the objectives (max 250 words). Experience within the BBP membership is that this scoring is not consistent between years and where consistent wording has been provided by a participant in answering a question (such as Question 1.1), the points awarded have differed. There is also no clear pattern in the change in scoring, both up and down, or detail to how scoring is carried out. This inconsistency and lack of transparency has potential to undermine the credibility of the Survey if the reasoning for the change and how qualitative answers are scored are not understood by participants.

BBP members

Aberdeen
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Blackstone
British Land
bruntwood
CADOGAN
CANARY WHARF GROUP PLC
Capital & Regional
CLS Holdings plc
CORDING REAL ESTATE GROUP
Deutsche Asset & Wealth Management
GROSVENOR
Hammerson
HERMES INVESTMENT MANAGEMENT
intu
LandSecurities
LaSalle INVESTMENT MANAGEMENT
Legal & General Investment Management
LOW CARBON WORKPLACE Partnership
M&G REAL ESTATE
QUINTAIN
SEGRO WHERE BUSINESS WORKS
Shaftesbury
TH Real Estate
THE CROWN ESTATE
Transport for London
WORKSPACE

Editor

Christopher Botten
Programme Manager
Better Buildings Partnership

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The Building Centre
26 Store Street, London WC1E 7BT

info@betterbuildingspartnership.co.uk
www.betterbuildingspartnership.co.uk