



Countdown to the Minimum Energy Efficiency Standards
(MEES)

Guidance for CRE Investors and Landlords

March 2017

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Arbnco, formerly known as CO2 Estates has produced this guidance, providing a brief overview of the Energy Efficiency (Private Rented Property) (England and Wales) Regulations 2015, better known as the Minimum Energy Efficiency Standards or MEES and practical steps to help achieve compliance for commercial properties.

SECTION 2 - OUTLINE OF MEES REQUIREMENTS

Background

The Energy Act 2011 came into force on the 19 October 2011 and is the primary legislation for the MEES Regulations, made on the 26 March 2015. The MEES Regulations came into force on 1 October 2016

In relation to the non-domestic private rented sector, Part 3 of the Regulations contains the minimum level of energy efficiency provisions, which is currently set at an energy performance certificate (EPC) rating of at least band E.

Further MEES guidance for non-domestic properties was published by BEIS in February 2017.

The minimum level of energy efficiency provisions will mean that, subject to certain requirements and exemptions:

- a) from **1 April 2018**, 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 Regulations apply to all buildings that require an Energy Performance Certificate (EPC), and which fail to meet the 'minimum standard' rating of E or higher. If the property has a rating of F or G, the landlord will be required to install energy efficiency measures to bring the EPC rating up to E. If an E cannot be achieved, there is still a requirement to improve the property.

It is currently estimated that nearly 20 per cent of non-domestic properties in England and Wales will be classed as sub-standard, failing to meet the minimum energy efficiency standard introduced by the regulations and will therefore require expenditure to ensure compliance

Failure to comply with the regulations could have significant implications on business continuity as landlords will not only be prevented from granting new leases (including renewals), but could also face financial penalties with breaches being published in a public register.

New Leases & Renewals: 1 April 2018

Unless an exemption applies, from 1 April 2018, the owner of a property with an EPC rating of F or G must not grant a new lease or renew an existing lease for that property, until works have been carried out to improve the energy efficiency in line with the requirements of the regulations.

All Leases & Buildings: 1 April 2023

Unless an exemption applies, from 1 April 2023, the owner of a property with an EPC rating of F or G must not continue to let out that property until works have been carried out to improve the energy efficiency in line with the requirements of the regulations.

Implications for Owners, Investors and Funders

For property owners, the regulations will require landlords to have a greater focus on the energy efficiency standards of a building and will result in some landlords having to make significant upgrades to their assets to ensure that they remain lettable and the capital value is not affected.

For funders and investors, there will be a greater emphasis on borrowers actively managing their real estate portfolios to ensure compliance with the regulations and that any required action is taken early or promptly to prevent a void in rental income or to mitigate any impact on market value. Many funders are including specific requirements in this regard.

Exemptions

There are some exemptions to the regulations, where a landlord of a sub-standard property (with an EPC rating of F or G) will be allowed to let or continue to let the property without undertaking the required energy efficiency improvements in the following situations:

- **Lease Term:** Where the lease term is less than 6 months (unless the tenant has been in occupation for 12 months previously) or over 99 years.
- **Consents:** Where the consent of the occupational tenant is required to carry out the works and the tenant has refused to provide that consent, or the consent of any third party is required, but despite reasonable efforts by the landlord to obtain that consent it has been refused or granted subject to unreasonable conditions.
- **Economic Efficiency:** If the energy efficiency works proposed will not deliver a simple payback within seven years (meaning that the savings in energy costs over seven years will be less than the cost of carrying out the works).
- **Reduction in Capital Value:** If the landlord obtains a report by an independent surveyor stating that the energy saving improvements, if made, would reduce the

capital value of the property by 5% or more.

- **Negative Impact on the Fabric:** If the landlord obtains a report by an independent installer of energy improvement works advising that the proposed work(s) in question are not appropriate due to the potential negative impact on the fabric of the building.
- **EPC Exempt:** Properties exempt from the requirement to obtain an EPC, e.g. buildings with existing permission to demolish, temporary buildings with a useful life of two years or less, places of worship and listed buildings, where such listing is visible on the Heritage England web site.
- **Temporary Exemption:** The purchaser of any sub-standard building which is let, will have a grace period of 6 months in which to carry out the works necessary to bring the building up to the required E rating.

Exemptions Register

To be able to rely on any exemption, the landlord must register details of the exemption with the supporting information.

The Exemptions Register will be available from 1 April 2017, but there is no requirement to lodge anything until 1 April 2018. Certain details will be publicly available. It will hold details of the property, the landlord, the exemption relied upon, the EPC and the date of registration.

A registered exemption will remain valid for five years (or until the end of the current tenancy).

An exemption cannot be transferred on sale or transfer. The new owner or landlord must attempt to comply with MEES or lodge a new exemption.

SECTION 3 - ENFORCEMENT AND PENALTIES

The Regulations will be enforced by Trading Standards. If the enforcement body suspects a landlord has breached the Regulations at any time in the preceding 12 months, a compliance notice will be served on the landlord requesting further information. If the notice is not complied with, or the information provided doesn't satisfy the enforcement body that an exemption applies, a penalty notice may be issued. The building must still be brought into line with the regulations through improvement measures.

The penalties may be financial or 'publication' in nature, or both. A publication penalty is a notice in the Exemptions Register that a breach has occurred. This Register will have certain areas which are publicly available. The financial penalties imposed are set out below:

Infringement	Penalty
Providing false or misleading information in respect to a claimed exemption.	£5,000
Failing to respond to a compliance notice	£5,000
Non-compliance < 3 months	Greater of £5,000 and 10% of the rateable value (capped at £50,000)
Non-compliance > 3 months	Greater of £10,000 and 20% of the rateable value (capped at £150,000)

SECTION 4 - RECOMMENDED APPROACH AND GUIDANCE TO MEES COMPLIANCE

The countdown to MEES compliance has started and landlords need to plan ahead to reduce any void letting periods or exposure to financial penalties.

Many organisations are undertaking portfolio audits, to identify 'at risk' properties currently sitting within the F and G rating band. Others are additionally including E rated properties, particularly those where EPCs were originally undertaken between 2008 and 2010, as EPCs have a 10-year lifespan, these may well fall into the F and G category when they are legally required to be renewed.

If a voluntary EPC is undertaken and lodged, it does not fall under the MEES Regulations.

Arbnco has direct experience through validating clients' existing EPC ratings that there are many cases of incorrect EPC ratings. In some cases, up to 80% of the E, F and G ratings can be improved to 'out of risk' purely by undertaking a new and accurate EPC.

All landlords will potentially be affected by the MEES regulations, irrespective of the size and nature of their portfolios and early action is advised to mitigate the impact. Similarly, for funders and investors in real estate, attention should be paid to the potential consequences of the regulations in terms of void rental periods, financial penalties and the capital value of their real estate portfolios.

Any owner will want to ensure that when they let a property, that it complies with the regulation at the end of the lease and that any work that the tenant undertakes does not impact the EPC rating detrimentally. Equally, the tenant will not want the owner to use the regulations as a strategy to get them to pay for improvements that would upgrade the rating of the EPC when the serviceable life of the building systems is still valid.

It would be advisable for the building owner if possible to take control of the EPC process so that they can ensure compliance and accuracy of the EPC rating.

Steps to Achieving MEES Compliance

- 1 Portfolio Review:** identify properties with no EPC, review lease renewal dates and decide whether a new EPC is required.
- 2** Confirm that 'at risk' properties, i.e. F and G EPCs are really F and G by undertaking new EPCs to provide accurate and dependable ratings before undertaking any retrofit works.
- 3** Identify means of retrofitting 'at risk' properties to achieve an E rating or better and assess the cost of compliance. Review impacts of future refurbishments and planned preventative maintenance (PPM) schedules.
- 4** Incorporate energy efficiency improvements into retrofit and PPM schedules.
- 5** Update leases, tenant fit-out and dilapidations processes to allow for appropriate provisions for the landlord/owner to continue to comply with the requirements of MEES.

