

Minimum Energy Efficiency Standards and Energy Performance Certificates for Commercial Rental Property

May 2021



By Fiona
Larcombe

Changes proposed in the government's 2021 consultation

As part of its carbon reduction strategy, the government is consulting on proposals to tighten the energy performance of commercial rented buildings. The consultation is open for responses until 9 June. Although the government does not expect to publish its final position until later this year, the move towards higher EPC ratings seems inevitable, so both owners and occupiers of commercial rented buildings should start thinking about what this means in practice now.

Summary:

- Minimum EPC rating for commercial rented buildings to go up to C by April 2027 and B by April 2030.
- EPCs to be compulsory for all commercial rented buildings within the scope of MEES and to be produced for a central register, with enforcement moving away from the point of letting.
- EPCs to be required for listed buildings and those in conservation areas.
- Extension of time for enforcement to allow for tenant fit out works on shell and core lettings.

What are the rules now?

- Since 1 April 2018, it has been unlawful to grant new lettings of commercial property in scope of MEES without an EPC of E or higher.
- From 1 April 2023, existing leases (i.e. any granted before 1 April 2018 and still in force) come within MEES and it will be unlawful to continue letting commercial property without an EPC of E or higher.
- EPC obligations fall on the landlord, not the tenant.
- Potential loopholes:
 - MEES do not bite if there is no EPC for the property, so there is no incentive to get one (or renew an expired one) until necessary for a new letting.
 - It is not clear whether listed buildings or buildings in conservation areas need an EPC, so not clear if they are caught by MEES.
 - Although there are maximum penalties of £5k for not having an EPC when required and £150k for letting in breach of MEES, enforcement is by local trading standards and is patchy, largely because there is no reliable source of data.

- “Comfort” for landlords:
 - Only required to do works that are “cost-effective” because doing them will achieve expected savings in energy bills over 7 years at least equal to the cost of the works (the 7 year payback test) – but must get three quotes as evidence.
 - Not obliged to achieve a higher EPC rating than is possible by doing all the “cost-effective” works.
 - May be eligible for a 5 year exemption, for example if the landlord may not do the works without consent (e.g. from the tenant) and that consent is not granted.
 - Additional 6 month temporary exemptions for new/involuntary landlords (e.g. on purchase, inheritance or on grant of a lease by court order).

Which lettings are NOT in the scope of MEES?

- Short leases - less than 6 months, unless there has been continuous occupation for 12 months
- Long leases - 99 years or more
- Occupational licences

What would change under the proposals?

- EPCs to be compulsory for all commercial rented buildings within the scope of MEES, including listed buildings and those in conservation areas. Expired EPCs would have to be renewed and it would be compulsory to get a new EPC after improvements are made. Landlords will also be obliged to provide letting agents with a valid EPC before a property is put on the market.
- Two stage hike in minimum EPC rating required:
 - 1 April 2027 – minimum C rating
 - 1 April 2030 – minimum B rating
- Valid EPC to be produced and registered 2 years before each compliance deadline, creating two “compliance windows”:
 - 1 April 2025 (with improvements by 1 April 2027 if required to get to EPC C)
 - 1 April 2028 (with improvements by 1 April 2030 if required to get to EPC B)

- Exemptions to be reviewed at the start of each compliance window (i.e. April 2025 and April 2028), with evidence submitted if required.
- Enforcement would move away from the point of letting and focus on compliance windows. Penalties would stay the same as they are now. Not yet clear what will happen in relation to enforcement after 2030, e.g. if a new tenant's fit out took a property below EPC B.
- For shell and core lettings, landlord would be able to register a temporary exemption to stop enforcement until the tenant had been in occupation for 6 months, to allow time for tenant's fit out. This is intended to solve the problem of poor EPC ratings for shell buildings. In practice, this would mean landlords wanting to impose new contractual obligations on tenants to fit out to an agreed specification (or by reference to the minimum EPC rating required) and within 6 months – either in agreement for lease or lease.
- Vague suggestion that landlords and tenants should have more obligations to co-operate and that there should be new duties imposed on tenants. No detail at this stage and note this would require primary legislation.
- There will be a simplified calculator to help landlords assess the 7 year payback test, removing the need for three quotes in most cases. As part of this, landlords would be required to undertake a suggested package of cost-effective measures.

Implications for leases and agreements?

- Tighter obligations on tenants in agreements to lease, in relation to specification and timing of work, with the right for the landlord to go in to do work and recover costs if the tenant is in breach?
- Tighter control of tenant alterations, in relation to impact on EPC rating and possible need for a new EPC.
- More collaborative and flexible approach to yielding up/reinstatement, to avoid adverse impact on EPC if fit out is removed. Could apply on exercise of break options as well as at the end of the term.
- Look at indemnities, to ensure landlord is protected if EPC falls below minimum required level as a result of tenant breach?
- Right for landlord to enter to carry out works required to improve EPC rating between now and 2030.
- Right for landlord to recover costs via service charge? Likely to be controversial and will have to be negotiated.

- Impact on common tenant amendments excluding any liability for such costs – even if these are agreed now, it may be wise to include a carve out in case new law imposes a duty on tenants. This may be difficult to negotiate, given the current proposals are vague.
- Rent review – assumption that property meets minimum level required to be lawfully let.
- Scope for leverage on re-gears of existing leases – landlords may require stronger drafting on EPCs (and other sustainability issues) in return for changes requested by tenants like pandemic rent cessers, switch to turnover rent, new break rights etc.

For further information please contact your usual Maples Teesdale contact or:

Fiona Larcombe

E: flarcombe@maplesteesdale.co.uk

T: 020 3465 4366