COMMERCIAL LEASES: A LEGAL INSTRUMENT TO DELIVER HIGHER PRODUCTIVITY OF GREEN COMMERCIAL BUILDINGS

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1 INTRODUCTION

Vast numbers of the commercial buildings in Australia are occupied not by the owners of these buildings, but by tenants. Because of this, there is a need for a legal relationship to govern the rights, duties, responsibilities and obligations of the tenants and the owners of these buildings. This points us towards the private legal instrument of a 'Lease'. A lease is designed to reflect the agreement that has been (or will be) entered into by two or more parties to govern the operation, use, and management of the premises. It is for this reason that a lease is arguably the most important legal instrument to govern the ongoing use and operation of commercial premises.

A lease can provide a powerful tool that can be used to influence directly the building's sustainability, both in operation and through decommissioning. Understanding this potential, a number of commercial leases are now taking on a 'green tinge' to reflect the growing importance of issues relating to climate change and sustainable development. However, such practices are not commonplace and even when 'green' terms are incorporated into a lease they are often used to supplement the conventional terms of a lease. Hence, the disconnect between the potential of leases to assist with creating a more sustainable built environment and its current failure to do so is the focus of this review.

The use of a lease to influence the sustainability of commercial buildings has been investigated in two steps. The first step was to consider the available literature, both from Australia and from overseas, on the role of leases to promote the sustainability of commercial buildings. This step includes consideration of the current regulatory position in Australia governing green commercial buildings. The second step was to consider how particular features of a lease could be used to encourage the sustainability of commercial buildings.

2 SUMMARY OF LITERATURE REVIEW

The following provides a summary of the seminal legal literature on the sustainable use and management of commercial buildings from Australia and overseas. In addition, and by way of context, this review also considers the laws that exist in Australia that are designed specifically to support the sustainable use and management of commercial buildings.

2.1 THE LAW IN AUSTRALIA TO REGULATE THE COMMERCIAL BUILT ENVIRONMENT

In 2006, the Commonwealth Government released the *Energy Efficiency in Government Operations* (EEGO) policy.[1] This policy mandates that premises are leased by or from the Commonwealth Government must include certain provisions that promote the sustainable use and management of the premises. The EEGO policy builds on the proposal that was contained in Stage 1 of the implementation plan of the National Framework for Energy Efficiency that was published in December 2004.[2] To facilitate compliance with the EEGO policy, the Commonwealth Government developed the 'Green Lease Schedule'.[3] The Green Lease Schedule contains the specific terms that must be included in leases in which the government participates in order to comply with the EEGO policy. The Green Lease Schedule promotes the sustainable use and management of the buildings to which it relates by setting a minimum ongoing operational building energy performance standard, which is measured by the National Australian Built Environment Rating Scheme.[4]

While the EEGO policy reflects the initial step towards leases that facilitate the sustainable use and management of commercial buildings, it was not until 2010 that mandatory laws were introduced that applied these concepts more broadly. This occurred with the passage of the *Building Energy Efficiency Disclosure Act 2010* (Cth) (BEED Act) and its associated regulations and determinations.[5] The BEED Act operates by requiring that from 1 November 2010 a corporation must not offer or invite offers to sell, let or sublet a prescribed building unless a valid and current Building Energy Efficiency Certificate (BEEC) is obtained and registered in respect of that building.[6] A BEEC is a certificate that sets out the energy efficiency rating for the building (or an area of a building), an assessment of the energy

[1] 'Energy Efficiency in Government Operations Policy' (Department of the Environment and Water Resources & the Australian Greenhouse Office, 2006).
[2] 'Statement on National Framework for Energy Efficiency Overview Plan of Stage One Measures 2005 – 2007' (Ministerial Council on Energy, 2004).
[3] More information about the Green lease schedule can be found at: *Green lease schedule* (Australian Government <http://climatechange.gov.au/government/initiatives/eego/green-lease-schedule.aspx>
[4] NABERS is a performance-based rating system for existing buildings. It operates by rating a building on 'its measured operational impacts on the environment, and provides a simple indication of how well you are managing these environmental impacts compared with your peers and neighbours' (see: *NABERS* (NSW Office of Environment and Heritage <http://www.nabers.com.au/>).
[5] *Building Energy Efficiency Disclosure Act 2010* (Cth); *Building Energy Efficiency Disclosure Regulations 2010* (Cth); *Building Energy Efficiency Disclosure (Disclosure Affected Buildings) Determination 2010* (Cth); *Building Energy Efficiency Disclosure Determination 2011* (Cth).
[6] *Building Energy Efficiency Disclosure Act 2010* (Cth), s 11.

efficiency of the lighting for the building (or area of the building) and any other matters determined under the legislation.[7] The BEED Act applies only to buildings that are used or capable of being used as an office in excess of an area of 2000 square metres.[8] It does not apply to buildings that a strata titled and are less than two years old.[9] Failure to comply with the requirements of the BEED Act will attract civil penalties.[10]

The BEED Act represents the sum total of the mandatory measures that the Commonwealth Government has developed that specifically encourage the sustainable management of commercial buildings. While the BEED Act may be considered a soft touch, it must be noted that the BEED Act is not the end result. Rather, according to the Commonwealth Government, it is the first 'step in the right direction'.[11] Therefore, as the Government continues to respond to the growing imperative to reduce greenhouse gas emissions, including through the newly devised carbon pricing mechanism, the sector should expect further regulatory developments that will mandate the more sustainable use and management of commercial buildings.

2.2 DOMESTIC AND INTERNATIONAL LITERATURE REVIEW

From an Australian perspective, efforts by legal practitioners and academics to use leases to affect the sustainability of commercial buildings has emerged from within the confines of the regulatory framework of the National Framework for Energy Efficiency, the EEGO policy and the accompanying green lease schedules. One of the first pieces of literature to emerge in relation to the application of green leases in Australia was published at around the same time that the National Framework for Energy Efficiency was released, in 2004.[12] The central focus of this review considered the role of green leases in the commercial property sector and, in particular, the strategies for '*achieving consensus between a landlord and tenant in introducing [concepts of sustainability] into commercial leasing arrangements*'.[13] Despite the seminal nature of this work, the development of Australian literature since then has been sporadic, with very few articles extending the work presented in the 2004 article.[14] While

[7] *Building Energy Efficiency Disclosure Act 2010* (Cth), s 13.
[8] *Building Energy Efficiency Disclosure Act 2010* (Cth), s 3.
[9] *Building Energy Efficiency Disclosure (Disclosure Affected Buildings) Determination 2010* (Cth), ss 4-5.
[10] *Building Energy Efficiency Disclosure Act 2010* (Cth), ss 11, 12(6) and 15.
[11] The Hon Greg Combet: Building Energy Efficiency Disclosure Bill 2010 (Cth), House of Representatives, Second Reading Speech, Hansard, 18 March 2010, p 2928.
[12] Tim Power, Rebecca Campbell and Brad Jessup, 'Lease arrangements for green commercial buildings' (2004) 19(3) *Australian Property Law Bulletin* 29.
[13] Tim Power, Rebecca Campbell and Brad Jessup, 'Lease arrangements for green commercial buildings' (2004) 19(3) *Australian Property Law Bulletin* 29, 29.
[14] See: Sharon Christensen and Bill Duncan, 'Green leases - A new era in landlord and tenant cooperation' (2007) 15 *Australian Property Law Journal* 54; Craig Roussac, Caitlin McGee and Geoff Milne, 'Changing the culture of commercial buildings in Australia: The role of green leases' (From the Proceedings of the World Conference on Sustainable Buildings, 2008); Tim Power, 'Building Green' (2008) *Law Institute Journal* 42; Sharon Christensen and Bill Duncan, 'Green leases - Becoming a reality' (2010) 19(1) *Australian Property Law Journal* 30; William D Duncan, *Commercial Leases in Australia* (Lawbook Co, 6th ed, 2011); 'Green leases' in *Australian Tenancy Practice and Precedents* (LexisNexis, 2011). For the articles that have extended our understanding of leases beyond the 2004 article see: Sharon

slightly more consideration has been given to the role of green leases in overseas jurisdictions – namely in the United Kingdom, Canada and the United States – there is low coverage of the topic in the legal literature.[15]

The term 'Green lease' is becoming known as a lease that seeks to reduce the environmental impact of commercial buildings, such as reducing the greenhouse gas emissions by reducing demand for fossil fuels through increased energy efficiency.[16] To underpin achieving such objectives, a 'green lease' needs to contain certain related obligations. This can be done by both the inclusion of new provisions and by amending existing terms, supported by a cooperative approach to property management, where the lessee and lessor work together to use and manage the premises sustainably.[17]

An emerging example of an effective new provision is the incorporation of an Energy Management Plan (EMP) into to the lease.[18] An EMP is designed to express specific objects related to energy management to which the lessor and lessee wish to subscribe in order to reduce the fossil energy consumption of the building, resulting in a reduction of the associated greenhouse gas emissions. Therefore, an EMP can form a central part of a 'green' lease, and can contain a range of features, including:[19]

- a definition of the aspirations of both the lessor and lessees to use best endeavours to meet the prescribed targets and objectives;[20]
- details of the various types of energy being consumed in the building (such as electricity generated from both fossil fuel and renewable options, natural gas, and onsite energy generated from both fossil fuel and renewable options);[21]
- identification of energy consumption targets for the building (or a particular tenanted portion of the building) for a specified period;[22]
- a description of how energy is being monitored in respect of common usage and individual usage;[23]

Christensen and Bill Duncan, 'Green leases - A new era in landlord and tenant cooperation' (2007) 15 *Australian Property Law Journal* 54; Sharon Christensen and Bill Duncan, 'Green leases - Becoming a reality' (2010) 19(1) *Australian Property Law Journal* 30; William D Duncan, *Commercial Leases in Australia* (Lawbook Co, 6th ed, 2011).

[15] See the references set out in the bibliography for international sources.

[16] See the references set out in the bibliography for international sources.

[17] Sharon Christensen and Bill Duncan, 'Green leases - A new era in landlord and tenant cooperation' (2007) 15 *Australian Property Law Journal* 54, 54; Susan Bright, 'Drafting green leases' (2010) 6 *Conveyancer and Property Lawer* 498, 501; ;Sharon Christensen and Bill Duncan, 'Green leases - Becoming a reality' (2010) 19(1) *Australian Property Law Journal* 30, 33.

[18] Sharon Christensen and Bill Duncan, 'Green leases - Becoming a reality' (2010) 19(1) *Australian Property Law Journal* 30, 35; William D Duncan, *Commercial Leases in Australia* (Lawbook Co, 6th ed, 2011), 458-459.

[19] Katherin Oberle and Monica Sloboda, 'The Importance of 'Greening' Your Commercial Lease' (2010) 35(1) *Real Estate Issues* 32, 35.

[20] 'REALpac Office Greenlease: National Standard Lease for Single-Building Projects - 1.03-2010' (Real Property Association of Canada, 2010)., sch E.

[21] Sharon Christensen and Bill Duncan, 'Green leases - Becoming a reality' (2010) 19(1) *Australian Property Law Journal* 30, 36.

[22] Katherin Oberle and Monica Sloboda, 'The Importance of 'Greening' Your Commercial Lease' (2010) 35(1) *Real Estate Issues* 32, 35. 'REALpac Office Greenlease: National Standard Lease for Single-Building Projects - 1.03-2010' (Real Property Association of Canada, 2010). sch E.

– a description of the nature and extent of energy consumption reduction measures being implemented in the building;[24]

– details of specific protocols for the recording, keeping and dissemination of data obtained through the monitoring process to ensure that the prescribed targets and objectives are met;[25] and

– an indication of the short, medium and long-term goals in relation to energy reduction.[26]

It is recommended that an Energy Management Committee (EMC)[27] be created and charged with monitoring compliance with the EMP.[28] The members of the EMC must represent the interests of both the tenant and the lessee so that there is a level of equality between the parties to the lease. Typically the EMP (and the EMC) are the most significant new obligation in a 'green lease' and is then complemented by a range of variations to existing terms, namely: rent and rent review, repairs and alterations, payment of outgoings, and provisions on assignment and subletting (as outlined in Table 1).

Table 1: *A sample of potential features of green leases for commercial buildings*

Feature	**Description of modification**
Rent and Rent Review	Under a standard lease, the level of rent and the process to review the rent levels do not include consideration of the tenant's performance, or the performance of the lessor. However, in a green lease these issues would be linked to the terms of the Energy Management Plan. Therefore, if through the prudent energy use of the tenant the outgoings of the building decrease, then this could be reflected in the reconsideration of the rent level.
Repair and alterations	A standard lease commonly permits the tenant/lessee to make alterations or additions (although not usually of a structural nature) with the consent of the lessor. Hence, as part of a green lease items could be included that relate to the type of materials

[23] Tim Power, 'Building Green' (2008) *Law Institute Journal* 42, 44; 'Green Lease Schedules Guidance Notes' (Australian Government, 2010), 22 and 25.
[24] 'REALpac Office Greenlease: National Standard Lease for Single-Building Projects - 1.03-2010' (Real Property Association of Canada, 2010), sch E.
[25] Tim Power, 'Building Green' (2008) *Law Institute Journal* 42, 44; 'Green Lease Schedules Guidance Notes' (Australian Government, 2010), 44.
[26] Katherin Oberle and Monica Sloboda, 'The Importance of 'Greening' Your Commercial Lease' (2010) 35(1) *Real Estate Issues* 32, 35; 'REALpac Office Greenlease: National Standard Lease for Single-Building Projects - 1.03-2010' (Real Property Association of Canada, 2010), sch E.
[27] Sharon Christensen and Bill Duncan, 'Green leases - Becoming a reality' (2010) 19(1) *Australian Property Law Journal* 30, 37.
[28] Tim Power, Rebecca Campbell and Brad Jessup, 'Lease arrangements for green commercial buildings' (2004) 19(3) *Australian Property Law Bulletin* 29, 37.

Feature	Description of modification
	or technology used to make repairs or alterations that have demonstrated contributions to meeting the energy management plan. If the tenant failed to comply with such conditions, the lessor would not be held to be unreasonably withholding its consent.
Outgoings	In a standard lease, outgoings such as energy bills are generally charged separately from rent. Where a building contains multiple lessees, the outgoings are typically calculated by dividing the total outgoings for the buildings between each of the lessees in proportion to the area that they occupy. While this approach may be sound if all of the lessees have the similar energy consumption levels, if a tenant makes changes to lower its energy use, the terms of a green lease should reflect and reward this. This then acts as an incentive for further energy conservation efforts.
Assignment and subletting	Under a standard lease, assignment or subletting of a tenancy is permitted following the consent of the lessor. While a green lease would not necessarily change this obligation, it would be prudent to impose a condition on the assignment or the subletting that states that a lessor will only agree to such an activity if the assignee or sublessee agrees to comply with the energy management plan.

Together, these new and modified features of a lease to a large extent reflect how the legal literature has conceptualised the use of a lease to manage commercial buildings in a sustainable manner. Other than in a few cases,[29] the literature does not explore in detail how other conventional features of a commercial lease may be used to underpin the sustainability of a commercial building. Further, there is little focus on the concept of sustainability beyond the idea of energy management. The next part outlines how existing leasing arrangements may be able to promote further energy management.

[29] Tim Power, Rebecca Campbell and Brad Jessup, 'Lease arrangements for green commercial buildings' (2004) 19(3) *Australian Property Law Bulletin* 29; Sharon Christensen and Bill Duncan, 'Green leases - Becoming a reality' (2010) 19(1) *Australian Property Law Journal* 30; William D Duncan, *Commercial Leases in Australia* (Lawbook Co, 6th ed, 2011); Susan Bright, 'Drafting green leases' (2010) 6 *Conveyancer and Property Lawer* 498.

3 COMMERCIAL LEASES: THE UNTAPPED POTENTIAL TO SUPPORT A SUSTAINABLE BUILT ENVIRONMENT

This section considers a number of the prominent covenants of a conventional commercial lease and the potential for these covenants to be used to further sustainable outcomes. This analysis is designed to illustrate how, with some creative thought, some of the prominent terms of a lease may be used to underpin the sustainability of commercial buildings, including:

- payment of rent and outgoings;
- the covenant to repair and the right of the lessee to make alterations;
- break and relocation clauses; and
- the covenant for quiet enjoyment.

3.1 PAYMENT OF RENT AND OUTGOINGS

The principal covenant in every lease is widely considered to be the covenant to pay rent.[30] Where 'rent' is the compensation paid to the lessor by the lessee for the exclusive use and possession of the premises on the terms on which the property is leased.[31] Rent is in and of itself a relatively simple concept. However, the manner in which rent is calculated in a commercial lease presents some complications, such as it often being categorised as either 'gross rent' or 'net rent'. Gross rent refers to the concept where the rent and the outgoings are contained in a single amount (with outgoings including rates, taxes and other running costs of the building such as water and energy bills).[32] For a lease that adopts the net rental approach (which is the more common approach used in commercial leases), rent and outgoings are treated separately.

A further complication can arise from the determination of rent and outgoings in a commercial lease where the building has multiple tenants; a common occurrence in large commercial buildings. In this case, a net rental lease may note the outgoings payable by a particular lessee in proportion to their percentage interest of the leased building.[33] However, '*it does not follow that the [lessee] is in charge either of energy supply, or of how much energy is used*'[34] either in or by the building. While lessees in a multi-tenanted building can arrange for a direct supply of electricity, gas and/or water to its premises by direct metering,

[30] William D Duncan, *Commercial Leases in Australia* (Lawbook Co, 6th ed, 2011), 125. See also: Adrian J Bradbrook, Clyde E Croft and Robert S Hay, *Commercial Tenancy Law* (LexisNexis Butterworths, 3rd ed, 2009), 37.
[31] William D Duncan, *Commercial Leases in Australia* (Lawbook Co, 6th ed, 2011), 125.
[32] William D Duncan, *Commercial Leases in Australia* (Lawbook Co, 6th ed, 2011), 128.
[33] William D Duncan, *Commercial Leases in Australia* (Lawbook Co, 6th ed, 2011), 128.
[34] Susan Bright, 'Carbon reduction and commercial leases in the UK' (2010) 2(3) *International Journal of Law in the Built Environment* 218, 220.

the services that are provided to the common areas of the building and those that are controlled by the lessor (such as heating or air conditioning) remain outside of the control of a lessee.[35] As a result, a lessee, while potentially being able to control its own supply of energy, gas and water is still required to pay for any charges that relate to the energy supplied to the common areas and for those services that are controlled by the lessor.[36]

This situation has rarely lead to tension in the past, however this is changing due to the increasing costs of energy and water,[37] and the recognition that current consumption levels of energy and water are contributing to the generation of greenhouse gas emissions.[38] The latter challenge has led to regulation in Australia to assist the Australian economy with transitioning to a *'cleaner energy future'*.[39] As a result of these interrelated challenges, lessees are considering how to reduce their use of energy and water in order to operate their premises in a more efficient manner. While this may be so, according to Oxford Professor Susan Bright, '*the opportunity to change or upgrade technical equipment to "greener" technology is usually only available to the landlord as the equipment will not usually fall within the tenant's premises, and even if it does there will usually be restrictions in the lease preventing the tenant from making structural alterations*'.[40] Despite the scope for lessors to make the required changes, lessors have traditionally been reluctant to do so because it will not be the immediate beneficiary of these changes. It will therefore have to retrieve some of the costs through rent, which may 'take too long to amortise'.[41]

This tension reflects one of the most profound 'split incentives' affecting the sustainability of commercial buildings.[42] However, a range of additional incentives are becoming available, such as 'green' rating systems that provide third party endorsement of the green credentials of the buildings – creating the possibility of a rent premium for such premises. Further to the benefit of accrediting the green performance, the lease can also be used to mitigate the split incentive by including incentives and penalties for both the lessor and lessee relating to energy use. For example, as Christensen and Duncan point out '*if the lessee's prudence in the utilisation of the resources in the building assists in bringing down the overall*

[35] Susan Bright, 'Carbon reduction and commercial leases in the UK' (2010) 2(3) *International Journal of Law in the Built Environment* 218, 221.
[36] Susan Bright, 'Carbon reduction and commercial leases in the UK' (2010) 2(3) *International Journal of Law in the Built Environment* 218, 221.
[37] Edwin O'Young, 'Not Just a Carbon Hit on Electricity Prices' (Port Jackson Partners Limited, 2010)
[38] 'Report of the Prime Minister's Task Group on Energy Efficiency' (Prime Minister's Task Group on Energy Efficiency, 2010), 141.
[39] On 8 November 2011, the Australian Senate passed the *Clean Energy Bill 2011* (Cth) which is designed to give effect to a carbon pricing mechanism from 1 July 2012. This means that both houses of the Australian Parliament have now passed this bill together with 17 other accompanying bills that support Australia's shift to a cleaner energy future. A useful explanation of the regulatory changes created by this new law is set out in 'Securing a clean energy future – The Australian Government's climate change plan' (Australian Government, 2011).
[40] Susan Bright, 'Carbon reduction and commercial leases in the UK' (2010) 2(3) *International Journal of Law in the Built Environment* 218, 222.
[41] Sharon Christensen and Bill Duncan, 'Green leases - Becoming a reality' (2010) 19(1) *Australian Property Law Journal* 30, 33. See also: Michael Brooks, 'Green Leases and Green Buildings' (2008) 22 *Probate and Property* 23, 34 and 40.
[42] Susan Bright, 'Carbon reduction and commercial leases in the UK' (2010) 2(3) *International Journal of Law in the Built Environment* 218, 222.

operational costs, there is no reason why this should not be reflected in the amount of rental charged from time to time.'[43]

Hence, in order to reduce this split incentive the lease needs to create the conditions that encourage cooperation and engagement between the lessee and lessor to reduce energy demand in a way that rewards each for such efforts.[44] The importance of such cooperative engagement is illustrated by the following statement by Land Securities, one of the largest property developers and managers of commercial buildings in the United Kingdom, '*Land Securities cannot make significant reductions in building energy consumption, or reduce waste or improve recycling, without a high level of cooperation from the tenants. Its own case studies show that on their own, they can reduce energy usage in a building by maybe up to 10 per cent over 3 years through improved management, but with tenant buy-in they can achieve 15-20 per cent reductions in one year.'*[45]

Hence, a key part of overcoming the split incentive and encouraging reductions of energy consumption in commercial buildings is to ensure that efforts are rewarded appropriately. This can be difficult if energy charges for sub-tenants are simply calculated by dividing the total energy bill for the building among the various tenants in proportion to their use of the premises. In this case, a tenant that is actively reducing their energy demand will reduce the total energy bill for the building, and this reduced bill will then be shared across the tenants, substantially reducing the reward to the proactive tenant. This can be largely overcome through the use of sub-meters for electricity, gas and water, assuming again that the benefits of such infrastructure are shared between the tenant and lessor. However, it is difficult to attribute energy costs to tenants from common areas and for services those that are managed by the lessor for all lessees (such as air conditioning and heating).[46]

It is clear that covenants relating to rent and outgoings may be used to encourage the more efficient use of energy by both lessees and lessors in commercial buildings. However, these terms must be considered alongside other features of a lease, such as the covenant to repair and the right to make alterations.

[43] Sharon Christensen and Bill Duncan, 'Green leases - Becoming a reality' (2010) 19(1) *Australian Property Law Journal* 30, 38.
[44] Sharon Christensen and Bill Duncan, 'Green leases - Becoming a reality' (2010) 19(1) *Australian Property Law Journal* 30, 33. See also: Michael Brooks, 'Green Leases and Green Buildings' (2008) 22 *Probate and Property* 23; Susan Bright, 'Carbon reduction and commercial leases in the UK' (2010) 2(3) *International Journal of Law in the Built Environment* 218, 227-228.
[45] 'Owner-tenant engagement in responsible property investing' (UNEP Finance Initiative Property Working Group, 2009) <http://www.unep.org/sbci/pdfs/COP15-Owner-Tenant_UNEPFI.pdf>, 8.
[46] Sharon Christensen and Bill Duncan, 'Green leases - Becoming a reality' (2010) 19(1) *Australian Property Law Journal* 30, 33.

3.2 COVENANT TO REPAIR AND THE LESSEE'S RIGHT TO MAKE ALTERATIONS

The majority of commercial leases contain a covenant that requires the lessee to keep the leased premises in repair.[47] Even if such an express covenant is not included in a commercial lease (which would be very unlikely), this covenant would be implied by statute on the part of the lessee.[48]

The basic premise of the covenant to repair requires that the lessee must maintain the leased premises in good and substantial repair, order and condition, having regard to the condition, '*age, character and locality of the building*'[49] at the time that the lease commenced.[50] Hence the covenant to repair requires the lessee to hand back the leased premises to the lessor at the end of the lease in substantially the same condition as that which it was provided.[51] In determining whether this has occurred, often 'fair wear and tear' is expected. It is important to note, however, that under Australian law a lessee is not required to repair inherent defects in the building,[52] as this is the role of the lessor.

It is clear that the covenant to repair may support the effective management of a commercial building in a manner that contributes to its energy efficiency and potentially the enjoyment of the building by its occupants. This is because the covenant to repair obliges a lessee to maintain the state of the leased premises in at least the same condition as that which it was provided. Therefore, if the building (or part thereof) was originally designed and fit out in such a way as to improve the energy efficient operation of the building and the experience of its occupants, the lessee would necessarily be obliged to maintain the premises in a manner that would not detrimentally affect these features of the premises.

Further, to the extent that the lessee is required to make any repairs during the term of the lease to comply with this covenant, these repairs must consider the effect that it will have on the efficient operation of the building and the experience of the occupants so as not to undermine the original design of the premises.[53] If, however, the lessee does not comply with the covenant to repair, the lessor's investment and potential for future earning is undermined. If this were to occur, the lease may be used to pursue an action against the lessee for which it may incur legal penalties or sanctions.

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[47] William D Duncan, *Commercial Leases in Australia* (Lawbook Co, 6th ed, 2011), 195.
[48] *Conveyancing Act 1919* (NSW), s 84(1)(b); *Transfer of Land Act 1958* (Vic), s 67(1)(b); *Property Law Act 1974* (Qld), s 105(1)(b); *Real Property Act 1886* (SA), s 124(b); *Transfer of Land Act 1893* (WA), s 92; *Land Titles Act 1980* (Tas), s 66(b); *Land Titles Act 1925* (ACT), s 119(b).
[49] *Lurcott v Wakeley and Wheeler* [1911] 1 KB 905 at 915; [1911-13] All ER Rep 41.
[50] William D Duncan, *Commercial Leases in Australia* (Lawbook Co, 6th ed, 2011), 195.
[51] William D Duncan, *Commercial Leases in Australia* (Lawbook Co, 6th ed, 2011), 210.
[52] William D Duncan, *Commercial Leases in Australia* (Lawbook Co, 6th ed, 2011), 210. See also: Bradbrook, Clyde E Croft and Robert S Hay, *Commercial Tenancy Law* (LexisNexis Butterworths, 3rd ed, 2009), 285-286; Anthony P Moore (ed), *Commercial and residential tenancies: The laws of Australia* (Lawbook Co, 2009), 68.
[53] Sharon Christensen and Bill Duncan, 'Green leases - Becoming a reality' (2010) 19(1) *Australian Property Law Journal* 30, 39.

Closely related to the covenant to repair is the right granted to a lessee to carry out alterations to the premises. Whereas the covenant to repair is concerned with maintenance, the right to make alterations governs any future changes that a lessee may carry out to these premises. Similar to the covenant to repair, a lessor may only provide its consent to a lessee to make alterations if these alterations maintain or improve the energy performance of the building. To this effect, a provision in the lease concerning the right of the lessee to make alterations may note that the consent of the lessor will be deemed to be withheld where the lessee does not use materials that are consistent with and enhance the sustainable credentials of the building.[54]

Further, a lessor may also note that it will be deemed to be withholding its consent to any proposed alterations unless the lessee uses materials that are allergy free and recyclable. By invoking such restrictions, the lessor can maintain the experience of the building's occupants and can ensure that when the building is demolished, many aspects of the building will be able to be recycled.[55] This latter approach supports the management of commercial buildings in a sustainable manner from 'cradle to cradle'. This holistic approach can be further supported by the effective design of break and relocation clauses.

3.3 BREAK AND RELOCATION CLAUSES

A commercial lease will often contain a 'break clause' or, as it is referred to in Australia, a 'right to demolish or refurbish'. A 'break clause' permits the lessor to end a lease prematurely following a stipulated period of notice so that the lessor can retake possession of the premises for some specified purpose. This specified purpose often relates to the refurbishment or redevelopment of the premises.[56] A relocation clause is a term that is found in a retail lease that entitles the lessor to relocate the lessee's business provided sufficient notice has been provided by the lessor, adequate alternative premises are provided to the lessee and certain other statutory requirements are met.[57]

Despite break and relocation clauses being somewhat different in form and substance, they are designed to pursue a similar objective. That is, they are both designed to afford lessors the ability to enhance a building (or a portion of a building). More importantly, these conventional features of a lease reflect how leasing arrangements are important to govern not

[54] Sharon Christensen and Bill Duncan, 'Green leases - Becoming a reality' (2010) 19(1) *Australian Property Law Journal* 30, 39.
[55] Sharon Christensen and Bill Duncan, 'Green leases - Becoming a reality' (2010) 19(1) *Australian Property Law Journal* 30, 39.
[56] William D Duncan, *Commercial Leases in Australia* (Lawbook Co, 6th ed, 2011), 441. See also: Harold W Wilkinson, 'Break clauses in leases' (1994) 144(6673) *New Law Journal* 1636; Emma Slessenger, 'Precedent Editor's notes' (2011) 4 *Conveyancer and Property Lawyer* 264.
[57] For the other conditions relating to relocation clauses see: *Retail Leases Act 1994* (NSW), s 34A; *Retail Leases Act 2003* (Vic), ss 53-58; *Retail Shop Leases Act 1994* (Qld), ss 46C-46G; *Retail and Commercial Leases Act 1995* (SA), s 57; *Business Tenancies (Fair Dealings) Act* (NT), s 48; *Leases (Commercial and Retail) Act 2001* (ACT), ss 136-138. See also: Rory O'Connor, *Relocation wars: a matter of strategy for landlords* (2005) Gadens Lawyers <http://www.gadens.com.au/Publications-View.aspx?documentid=158>.

only the day-to-day operation of commercial buildings but also the much larger processes of operation, management, repair, demolition, and reuse of these buildings. In effect, this represents how conventional leases can further support the management of commercial property from 'cradle to cradle'.

The flexibility afforded to lessors under break and relocation clauses necessarily lends itself to improving the long-term sustainability of commercial buildings. These provisions allow lessors to end a lease prematurely (or cause lessees to be relocated) if they wish to upgrade, retrofit of demolish the building because its current design does not promote the efficient use of energy and water, which, in turn, detracts from the overall experience of the building's occupants.

Such outcomes may be able to be further enhanced by developing the cooperative relationship between the lessee and the lessor that was identified earlier. Under such a relationship, a lessee may wish to agree to enter into a new lease (where the lease was terminated) or a lease extension (where the lessee was relocated) following the refurbishment if the refurbished premises meet certain energy efficiency standards and are designed to enhance occupant experience. Such a term might offer the lessor some certainty that the building (or part thereof) will be leased following the refurbishment and, at the same time, will encourage the lessor to undertake the refurbishment in such a way as to enhance the sustainable design and operation of the building.

Therefore, the nature of break and relocation clauses may be recast in a commercial lease in order to extend the current governance of commercial buildings beyond the 'cradle to grave' paradigm to incorporate such a 'cradle to cradle' approach where redevelopments, refurbishments and ongoing leasing arrangements are contemplated in the terms of a lease.

3.4 THE COVENANT FOR QUIET ENJOYMENT

While the previously discussed covenants represent useful opportunities to pursue the sustainability of commercial buildings, they can also lead to new and unwanted tensions between the parties. Such tensions can include the case where the lessor may wish to operate the building in a particular way that achieved energy reductions but is potentially contrary to the beneficial experience of the occupants of the building. Consider, for example, the situation where a lessor reduces the use of air conditioning or heating in a building in order to improve the 'green' credentials of the building. However, by doing so it detrimentally affects the experience of the building's occupants. It is because of the potential for such a tension that a lease must be able to ensure that the experience of occupants is maintained despite the

pursuit of a more energy efficient building. This is the role of the covenant for quiet enjoyment.

According to the covenant for quiet enjoyment the lessor warrants that if the lessee pays the rent and performs and observes the covenants and conditions in the lease (such as the covenant to repair), the lessee may hold and enjoy the leased premises during the term without any interruption by the lessor.[58] While an express covenant for quiet enjoyment may often be linked to the payment of rent under a lease, the obligation of the lessor to ensure that it provides the lessee with quiet possession does not in fact depend on the continued payment of rent.[59] Rather, the obligations on the lessee to pay rent and the covenant on the lessor to give quiet possession are separate and non-related obligations.[60] For this reason, the law regards the covenant for quiet enjoyment as paramount to the operation of a lease. This point is reflected in the fact that even if such a provision were not expressly included in a lease, the law would imply such a covenant '*to the effect that the lessor, and those claiming through or under the lessor, would not disturb the possession of the lessee'*.[61]

The seminal case that affirms the importance of the covenant for quiet enjoyment to the maintenance of the building's internal environmental quality and the experience of the occupants of the building is *Hawkesbury Nominees Pty Ltd v Battik Pty Ltd*[62]. This case concerned a lease between (among others) Hawkesbury Nominees Pty Ltd (the lessor) and Battik Pty Ltd (the lessee). In the case, the lessee claimed that the lessor breached the covenant for quiet enjoyment because it interfered with an air system, which rendered the premises unfit for the purposes of a restaurant.[63] The lessee claimed that this breach occurred because, when the lessee's took possession of the premises, 'it was ventilated by an exhaust fan located in the basement. There was ducting from the kitchen to the fan and thence from the fan to the roof of the building'.[64] The lessor subsequently moved the exhaust fan. This then led to an increase in smoke and heat in the restaurant. Consequently, this led to part of the restaurant becoming unusable which, in turn, led to the reduction in profit for the lessee.

[58] William D Duncan, *Commercial Leases in Australia* (Lawbook Co, 6th ed, 2011), 225. See also: Adrian J Bradbrook, Clyde E Croft and Robert S Hay, *Commercial Tenancy Law* (LexisNexis Butterworths, 3rd ed, 2009) 233; Anthony P Moore (ed), *Commercial and residential tenancies: The laws of Australia* (Lawbook Co, 2009), 55. The covenant for quiet enjoyment 'is not an absolute covenant protecting a tenant against eviction or interference by anybody, but is a qualified covenant protecting the tenant against interference with the tenant's quiet and peaceful possession and enjoyment of the premises by the landlord or persons claiming through or under the landlord. The basis of it is that the landlord, by letting the premises, confers on the tenant the right of possession during the term and impliedly promises not to interfere with the tenant's exercise and use of the right of possession during the term' (see: *Kenny v Preen* [1963] 1 QB 499 at 511; [1962] 3 All ER 814).
[59] *Dowse v Wynard Holdings Ltd* [1962] NSWR 252 at 263; *Hawkesbury Nominees Pty Ltd v Battik Pty Ltd* [2000] FCA 185 at 50.
[60] *Dowse v Wynard Holdings Ltd* [1962] NSWR 252 at 263; *Hawkesbury Nominees Pty Ltd v Battik Pty Ltd* [2000] FCA 185 at 50.
[61] William D Duncan, *Commercial Leases in Australia* (Lawbook Co, 6th ed, 2011), 225.
[62] *Hawkesbury Nominees Pty Ltd v Battik Pty Ltd* [2000] FCA 185.
[63] *Hawkesbury Nominees Pty Ltd v Battik Pty Ltd* [2000] FCA at 3.
[64] *Hawkesbury Nominees Pty Ltd v Battik Pty Ltd* [2000] FCA at 6.

As a result, the court in this matter found that the covenant for quiet enjoyment had been breached.[65]

The reference to this case exemplifies how the covenant for quiet enjoyment has been used to protect the internal environmental quality of the premises and the experience of occupants within that building. For this reason, it is important that efforts by the lessee to improve the energy performance of the building take into consideration the potential impacts on occupants.

[65] *Hawkesbury Nominees Pty Ltd v Battik Pty Ltd* [2000] FCA at 49.

4 THE FUTURE OF LEASES TO UNDERPIN THE SUSTAINABILITY OF COMMERCIAL BUILDINGS

A commercial lease provides the foundation to govern the sustainable management, operation, upkeep, and redevelopment of commercial buildings. To some extent, commercial leases are already beginning to incorporate various provisions that are designed to encourage the 'green' performance of commercial buildings. In addition, many of the most fundamental covenants of commercial leases offer hidden opportunities to pursue the management of commercial buildings in a way that can encourage energy efficiency, improved occupant experience, and better internal environmental quality. However, more needs to be done in order to make these leases capable of effectively promoting sustainability within the commercial building space.

Arguably, the most important change that needs to occur is that commercial leases must be reconceptualised as cooperative commercial agreements that have as their principle object the sustainable management and use of commercial buildings. In effect, this means that the typical adversarial nature of such relationships must be changed to ensure that both lessor and lessee are operating to achieve the same premise: the sustainable use of the commercial built environment. By doing so, leases can be used to achieve 'win-win' outcomes between lessors and lessees, which will ultimately assist with the more sustainable management of commercial buildings.

In order to accelerate and expand the coverage of such positive outcomes, it may be the case that one must begin with a blank canvas from which a new lease can be designed. By doing so, one can avoid the shortcomings of traditional 'green' leases that merely use modified clauses to supplement existing covenants which do not properly reflect the importance that must be given to the concept of sustainability. .

5 FURTHER STEPS

It is clear that further research is required to reconceptualise the nature of a commercial lease of a 'green' building beyond the ad hoc recommendations that have been made to date by the available literature, which have been noted above. This may require research that considers the entire basis of the lessor and lessee relationship within the new sustainability regime being promoted by federal and state governments. This paper alludes directly to those specific matters of substance which any further study in this area would have to consider. However, any such further study would have to go much further in examining the relationship from the 'ground up' in order to support the 'cultural changes in business practices [that] are required'[66] to pursue a sustainable built environment. The necessity for this is warranted due to the lack of material available – both in Australia and overseas – within the leasing context.

[66] Sharon Christensen and Bill Duncan, 'Green leases - A new era in landlord and tenant cooperation' (2007) 15 *Australian Property Law Journal* 54, 65.

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