



CRC Energy Efficiency Scheme: Due diligence considerations for property transactions

Summary and Implications

With the introduction of the CRC Energy Efficiency Scheme (the CRC Scheme), further due diligence on property acquisitions should now be undertaken.

This briefing looks at some of the CRC due diligence issues that arise when acquiring property as an investment.

Market Overview

The Lettings Market

The lettings market has been slow to react to the potential cost implications of the CRC Scheme and there has been no consensus or market agreement on how participating landlords will deal with the scheme.

Whether landlords will generally seek to pass the CRC costs through to their tenants (along with any Revenue Recycling Payment) or whether they will treat the costs as a business overhead and absorb them as part of their operating costs (which itself may ultimately lead to higher rents) is not yet clear. Notwithstanding this, landlords that wish to re-charge such costs to their existing tenants also face the hurdle of whether the lease itself allows them to do so – the prevailing market view is that current standard lease provisions in most leases do not.

Some of the issues raised in this briefing will apply to tenants who are taking new leases or assignments of existing leases. However the main focus of this briefing is on the acquisition of investment property.

The Investment Market

The investment market is beginning to adapt to the CRC Scheme. Advisors will need to undertake additional due diligence to ensure that they obtain the necessary data to assist their clients with managing their CRC Scheme obligations.

Ask a question

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The CRC Energy Efficiency Scheme

You can also obtain further information on the CRC from the Climate & Energy pages on our website [here](#).

Click [here](#) for the Environment Agency's portal on the CRC Scheme.

The Real Estate team

To find out more about the team, and our capabilities [click here](#)

Participants in Phase 1 of the CRC Scheme

Participants in Phase 1 of the CRC Scheme should now be implementing internal audit systems to assess their energy usage for the current footprint year (1 April 2010 – 31 March 2011). This will assist in preparing their first Footprint Report (which broadly records which emissions are to be included within the CRC scheme for the phase) and the annual report (which provides a summary of the supplies and actual emissions) both of which are due by 31 July 2011. Remember, the CRC Scheme applies to virtually all fuels, not just electricity and gas.

Where investors are participants in Phase 1 of the CRC Scheme and now acquire additional property for which they are responsible for the energy supply (this is likely to be the case in owner-occupied property and multi-tenanted buildings) they will need to include details of this additional energy consumption within their reports.

On any new acquisition a purchaser should therefore be seeking additional information on and an understanding of factors such as:

- **Details of the existing arrangements for the provision of energy at the property** - In multi-let property, occupational tenants may in part be responsible for some of the energy supplies and purchasers should therefore obtain a breakdown of such responsibilities between the parties;
- **Details of the energy meters at the property** - Part of the qualification criteria for mandatory participation in the CRC scheme is having at least one half hourly meter settled on the half hourly electricity market. There are several types of meters in existence and it is important to identify the type of meter as this will also affect the participant's reporting obligations;
- **Copies of all energy supply agreements relating to the property** - A property may have a number of energy supply agreements in place and purchasers should ensure that copies of all such agreements are obtained. This will enable the participant to track the ongoing energy consumption. The purchaser can then begin to ensure that it holds sufficient CRC allowances to cover this consumption or at least be in a position to assess the additional CRC allowances required;
- **Details of the levels of energy consumption at the property** - Where information is not readily available, participants have recourse through the CRC order to obtain this information from third parties – see opposite. This information will assist the CRC participant in assessing the required number of CRC allowances it will need to purchase to cover the additional usage;
- **Whether CRC allowances are available for purchase from a seller** - A purchaser acquiring property from a fellow CRC Scheme participant may also be able to acquire the additional CRC allowances it may need in respect of the property. This trading aspect will apply once the initial sale of allowances has taken place and in due course the purchase of such allowances could form part of the terms of the purchase of the property;

CRC Scheme Registration

The CRC Scheme came into force on 1 April 2010 and the registration process for participating in the first phase expires on 30 September 2010.

With the deadline for registration of "Significant Group Undertakings" set for 30 June 2010 – registrations may well surge in the coming weeks.

CRC - Obtaining Energy Usage Information

The CRC Scheme Order 2010 includes various provisions to enable participants to obtain energy usage information from third parties.

- *Article 63* – enables participants to obtain details from authorised suppliers of the amounts of gas and electricity supplied.
- *Article 65* – requires a tenant to provide a landlord with reasonable assistance to comply with its obligations as a participant.
- *Article 67* – requires members of public bodies to provide the registered CRC participant with reasonable assistance to comply with its CRC obligations.

- **Copies of any energy audits, surveys or assessments carried out in respect of the property** - A number of consultants provide services to property owners to enable them to improve the energy efficiency of their portfolios. Where possible, purchasers should obtain copies of these reports. This will assist the purchaser to identify areas to improve energy efficiency and by implementing recommended measures should help to improve its position in the CRC Scheme performance table. This may ultimately provide the participant with a greater Revenue Recycling Payment for its efforts.

The availability of information will be key for CRC participants to manage their obligations and deal with the administration of the scheme.

Non-Participants in Phase 1 of the CRC Scheme

Non-participants in Phase 1 of the CRC Scheme will need to consider similar issues to participants. Whilst they may not immediately be concerned with CRC matters for Phase 1, Phase 2 is fast approaching and we are already within the qualification year for Phase 2 (1 April 2010 – 31 March 2011). Current non-participants will therefore need to consider whether the energy usage within their properties might be sufficient to require them to register for Phase 2 of the CRC Scheme.

It is also worthwhile for non-participants to raise similar enquires to participants on a purchase of a property because they may (in due course) dispose of their interest to a CRC participant.

In practice, having as much information to hand as possible will smooth the due diligence process on any subsequent sale.

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In instances where a property acquisition will bring a purchaser within the CRC Scheme, the net costs of compliance with the CRC Scheme will also need to be factored into the acquisition and the additional due diligence will assist in preparing for and focusing on this.

Conclusion

The property industry is currently adapting to the CRC Scheme. At present the BPF Commercial Property Standard Enquires do not include enquires on the CRC Scheme but these are being revised and new enquires are expected to be issued shortly. The City of London Law Society Certificate of Title has also yet to be adapted to consider the CRC Scheme but no timetable has been set for this. Advisers are busy updating their standard form reports and terms of engagement. Although the learning curve is steep, one thing is clear - CRC due diligence on property transactions should now be undertaken by purchasers and their advisors alike. This due diligence will be key to assisting purchasers with managing their existing or any potential future CRC obligations saving costs and time in the long run.

CRC – Key Phase 1 Dates (2010/2011)

- 30 June 2010 – Deadline for registration of Significant Group Undertakings.
- 30 September 2010 – Deadline for registration within the CRC Scheme.
- 31 March 2011 – Expiry of the initial Footprint Year.
- April 2011 – Fixed price sale of allowances at £12/carbon tonne.
- 31 July 2011 – Initial Footprint Report/Annual report due.

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