



**BUILDING  
UPGRADE  
FINANCE**

SOUTH AUSTRALIA

**TENANT  
CONTRIBUTION  
FAQ**

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# BUILDING UPGRADE FINANCE FAQs

## TENANT CONTRIBUTIONS

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## KEY TERMS

|  |   |
|--|---|
| <b>Building Upgrade Finance</b>                        | A finance product available to building owners to undertake environmental or heritage upgrades.   |
| <b>Building Upgrade Agreement</b>                      | The agreement between a building owner, finance provider and local council to use Building Upgrade Finance.   |
| <b>Building Upgrade Charge</b>                         | A local council charge against the land on which the building is situated that allows councils to collect repayments from the building owner and transfer them to the finance provider.   |
| <b>Environmental upgrade</b>                           | Upgrades that improve the environmental performance of a building.  |
| <b>Heritage upgrade</b>                                | An upgrade to a state or local heritage listed building that preserves heritage significance, addresses compliance with building rules or disability access, or allows ongoing occupation of the building.  |
| <b>Consent pathway for tenant contributions</b>        | Where the tenant and building owner negotiate a tenant contribution to upgrade works between themselves.  |
| <b>'No worse off' pathway for tenant contributions</b> | Where the building owner requires a tenant contribution towards upgrade works, provided the tenant will be 'no worse off' – i.e. the contribution will not exceed the utility bill savings to be made from the upgrade works. This pathway does not require tenant consent. |
| <b>Non-residential building</b>                        | A building predominantly used for non-residential purposes (e.g. commercial, industrial, agricultural).   |
| <b>Upgrade works</b>                                   | Either an environmental upgrade or heritage upgrade, or a combination of both.  |
| <b>Utility</b>   | The service that is being upgraded – e.g. water, electricity or gas.  |

## 1. What is Building Upgrade Finance?

*Building Upgrade Finance* is a finance product provided by private sector financiers to building owners for environmental improvements to existing non-residential buildings (i.e. commercial, industrial, agricultural etc.), or for restoration and upgrade of non-residential heritage buildings.

A wide range of environmental upgrades are eligible under Building Upgrade Finance including:

- Renewable energy (i.e. solar)
- Energy storage
- Air conditioning
- Electric Vehicle chargers
- Lighting
- Energy use optimisation
- Water efficiency and reuse systems
- End-of-Trip facilities (i.e. bike storage areas)
- Waste management systems
- Pollution control

In addition, for state or local heritage listed buildings<sup>1</sup>, the following heritage upgrades are eligible:

- Maintain, repair upgrade or reinstate heritage significance
- Comply with the Building Rules or the *Disability Discrimination Act 1992*
- Facilitate the ongoing occupation of the building.

In South Australia, Building Upgrade Finance was enabled through amendments to the [Local Government Act 1999](#) and [Local Government \(Building Upgrade Agreements\) Regulations 2017](#).

Similar products are available in Victoria (called Environment Upgrade Finance) and New South Wales.

<sup>1</sup> This includes buildings that are, or are part of, a State Heritage Place under the *Heritage Places Act 1993* or are designated as a place of local heritage under the *Development Act 1993* (or *Planning, Development and Infrastructure Act 2016* as applicable).

## 2. How does Building Upgrade Finance work?

Building Upgrade Finance is activated through a *Building Upgrade Agreement*<sup>2</sup> between a building owner, a finance provider and a local council where:

- the building owner agrees to undertake building upgrade works and repay the finance;
- the finance provider agrees to advance money to the building owner to fund the upgrade works; and
- the council agrees to declare a local council charge (called a *Building Upgrade Charge*) against the land on which the building is situated, collect repayments from the building owner and transfer them to the finance provider.

Repayments are collected from the building owner through the local council charge, via quarterly direct debits using the rates collection system and a separate rates notice. The repayments are then transferred by the council to the finance provider via electronic funds transfer.

Building Upgrade Finance is secured by the property (through the local council charge) rather than the building owner. This allows for finance providers to offer more attractive loan terms, resulting in a number of unique benefits as outlined in *Question 3*.

Building Upgrade Finance also provides a process for building owners and tenants to share the costs and benefits of upgrade works. Further information on this process is outlined in subsequent questions.

## 3. What are the benefits of Building Upgrade Finance for building owners and tenants?

Building Upgrade Finance is a tool that allows building owners and tenants to work together to unlock the benefits of upgrade works, including improved operating costs and working conditions, and to share the costs of the upgrade.

<sup>2</sup> The South Australian Government, in consultation with stakeholders, developed a *Building Upgrade Agreement template* that can be used by property, finance and local government sectors. Clauses 12-14 of the Building Upgrade Agreement template are mandatory for all Building Upgrade Agreements.

Building Upgrade Finance provides unique benefits for non-residential building owners compared with traditional finance which can assist to enable environmental and heritage upgrades, including:

- More attractive loan terms - including fixed quarterly repayments allowing businesses to maintain and potentially generate positive cash flow, and longer loan terms (10-20 years);
- No upfront capital is required so there is no impact on capital budgets;
- A very broad range of eligible upgrade works (as outlined in *Question 1*);
- If the property is leased, upgrade costs can be shared with tenants through a transparent process without having to renegotiate existing lease arrangements;
- If the property is sold, the remaining repayments can be passed onto the new owner (if all parties agree);
- Attraction and retention of tenants by providing a competitive, efficient workspace.

Building Upgrade Finance assists building owners to re-think asset strategies to retain or attract tenants or reposition a building asset for sale.

For tenants, Building Upgrade Finance can provide a range of benefits. Depending on the upgrades undertaken, benefits could include:

- Improved facilities i.e. bike storage facilities;
- Upgraded fixed equipment and lighting;
- Improved working conditions and amenity which can increase staff productivity and wellbeing;
- Reduced utility and / or operating costs;
- Contributions towards corporate social responsibility goals.

For tenants interested in improving the buildings that they occupy, Building Upgrade Finance can provide an opportunity to start discussions regarding improvements with their building owners.

## 4. When can a building owner seek a contribution from a tenant?

If a building owner undertakes upgrade works using Building Upgrade Finance on an eligible non-residential tenanted building, tenant contributions to the Building Upgrade Charge repayment can be considered.

Where upgrade works deliver financial benefits to the tenant i.e. through utility bill savings, the building owner can seek a contribution from the tenant. Where upgrade works do not deliver financial benefits to the tenant, the building owner may seek a contribution with the consent of the tenant. See *Question 5* for more information on the pathways for tenant contribution.

Contributions from the tenant can be recovered without having to renegotiate existing lease agreements, for example where the lease agreement was entered into prior to the execution of the Building Upgrade Agreement.

It should be noted that tenant contributions cannot be recovered until the associated upgrade works are complete.

## 5. How can a building owner seek contributions to an upgrade from their tenants under Building Upgrade Finance?

Building Upgrade Finance provides two pathways for the building owner (the lessor) to recover a contribution to the Building Upgrade Charge from the tenant (the lessee):

1. 'Consent' pathway where the tenant and building owner negotiate and the tenant agrees to pay a contribution to the upgrade cost; or
2. 'No worse off' pathway where the tenant is required to pay a contribution, provided the building owner has demonstrated that such a contribution will not exceed the tenant's cost savings resulting from the upgrade during the period to which the contribution relates. This pathway does not require tenant consent.

### EXAMPLE 1 - CONSENT PATHWAY:

A building owner and a tenant both agree that the façade and disability access of a heritage building they own/occupy needs to be upgraded. Both parties can agree to a shared contribution to the costs of the upgrade, even though the tenant may not see any utility bill savings from this work.

### EXAMPLE 2 - 'NO WORSE OFF' PATHWAY:

A building owner would like to undertake some energy efficiency works (e.g. LED lighting, a building management system upgrade, improvements to heating and cooling) on their building with tenant contributions. If the building owner is able to demonstrate to the tenant that their contribution would be equal to or less than the utility bill savings they will receive from the upgrade works, the building owner can require the tenant to contribute.

| PATHWAYS AVAILABLE                              | CONSENT | NO WORSE OFF |
|---|---------|--------------|
| Provides utility cost savings to tenant         | ✓       | ✓            |
| Does not provide utility cost savings to tenant | ✓       | X            |

A contribution to a Building Upgrade Charge is considered to be an outgoing expense in a lease.

Provisions regarding tenant contribution can be found at clause 12 of the [Local Government Act 1999](#) and clause 9 of the [Local Government \(Building Upgrade Agreements\) Regulations 2017](#).

## 6. What are the conditions of the 'no worse off' pathway to recover the tenant contribution to the Building Upgrade Charge?

To require a tenant to pay a contribution to a Building Upgrade Charge under the 'no worse off' pathway, the building owner must demonstrate that a

contribution to the Building Upgrade Charge will not exceed the tenant's cost savings resulting from the upgrade during the period to which the contribution relates. This must be done using a government-approved methodology (refer to [Q7](#)).

Under the 'no worse off' pathway, the building owner is also required to:

- notify the tenant of the amount of the contribution at least 30 days before the payment of the first contribution;
- include the estimate of cost savings for the tenant resulting from the upgrade in the notification, using the government-approved methodology;
- provide evidence of calculations of cost savings;
- provide the tenant with an annual report demonstrating the tenant cost savings, using the government-approved methodology, within three months from the end of the reporting period; and
- if the tenant cost savings were not achieved, credit the exceeded amount to the tenant (or provide a refund if the tenant requests this option) and reduce the future tenant contributions to the lesser amount to reflect the cost savings made.

The building owner and the tenant can agree if requirements (d) and (e) do not apply or are modified.

## 7. What is the government-approved methodology and where can I find it?

If the 'no worse off' pathway is followed to recover contributions from tenants, the building owner is required to use the government-approved methodology to estimate tenant cost savings.

The *'No Worse Off' Methodology for Estimating Tenant Cost Savings* (the Methodology) was Gazetted on 8 August 2017 and is available from the [Department for Environment and Water website](#).

The methodology provides for a robust pathway to estimate tenant cost savings whilst minimising the costs associated with its application. It uses a number of sub-methods to suit a wide range of environmental upgrades which result in cost savings from reducing gas, electricity and water use.

For example, a simpler approach may be applied for upgrades with more predictable performance outcomes (e.g. a lighting upgrade). More complex options are specified to suit more complicated upgrades requiring engineering models (e.g. an upgrade of an air-conditioning system).

It is recommended that suitably qualified individuals with relevant experience be engaged to undertake calculations using the methodology. Each sub-method provides examples of suitably qualified individuals to use the methodology for each type of upgrade works. A guide to help property stakeholders, consulting engineers and service providers better understand the methodology is also available at the [Department for Environment and Water website](#).

## 8. What happens if the reported tenant savings differ from the predicted tenant savings under the 'no worse off' methodology?

If the savings are greater than the predicted savings, the building owner is not entitled to recover any additional contribution for any excess savings made by the tenant in the reported period.

If the predicted tenant cost savings were not achieved within the reporting period, the building owner must credit the tenant with the exceeded amount (or provide a refund if the tenant requests this option) and reduce the future tenant contributions to this lesser amount to reflect the cost savings made.

## 9. Does the tenant need to receive a copy of the Building Upgrade Agreement?

If a tenant asks for a copy of the Agreement, the building owner must provide it irrespective of whether a contribution has been determined by consent pathway or by the 'no worse off' pathway.

## 10. Can tenant contribution be recovered for heritage upgrades?

Heritage upgrades may not result in utility cost savings for the tenant, however there are other benefits to tenants such as improvements to facades, fire safety and disability access.

Under the 'no worse off' pathway, heritage upgrades that do not deliver utility cost savings cannot be recovered from tenants.

Under the 'consent' pathway, the tenant may agree to pay a contribution to the Building Upgrade Charge even though the upgrade does not necessarily deliver any utility cost savings.

## 11. Can residential tenants in mixed use buildings be required to pay a contribution to the Building Upgrade Charge?

Building Upgrade Finance does not extend to the residential sector. Residential tenants in mixed use buildings cannot be required to pay a contribution to the Building Upgrade Charge.

## 12. How does the 'no worse off' methodology apply to different types of leases?

Under the 'no worse off' methodology, contributions from tenants to the Building Upgrade Charge can only be recovered if the tenant normally pays, or contributes to the payment of, the relevant utility costs where savings are to be made from the upgrade works.

### NET LEASE

A 'net' lease means the rent excludes operating costs/outgoings and these are charged on top of rent. These extra costs will vary from lease to lease but often include common area energy and water bills. The building owner will receive these bills, and then

charge all or a proportion of the bills to the tenant to pay on top of their rent.

Under a net lease scenario, the tenant contribution is calculated on the basis of the tenant's share of the utility bill set out in their lease agreement. For example, if the tenant pays 20% of the energy bill, the building owner can seek 20% of the total cost savings resulting from the upgrade to the tenant.

Under a net lease, electricity for lights and power within tenancies is often separately metered. In this case tenants purchase this electricity directly from a retailer of their choice, which is considered a separate utility under the Methodology. If the tenant purchases electricity directly from a retailer, the tenant contribution is calculated based on the savings to that utility.

## GROSS LEASE

A 'gross' lease is a fixed amount lease. This means that operating costs/outgoings of the building are built into the rent. These costs typically include utilities used in common areas such as air conditioning, lifts, foyer and carpark lighting, toilets, etc.

For utilities included in the gross lease, because no operating costs are passed through to the tenant by the building owner, the building owner keeps the savings from the upgrade. Therefore, under the 'no worse off' pathway, the tenant cannot be required to pay a contribution to the Building Upgrade Charge. Instead, the building owner may wish to use a 'consent pathway' where the tenant agrees to pay a contribution.

However, under a gross lease, utility use in the tenant space may be separately metered and purchased by the tenant either through the building owner or directly from a retailer. If the tenant purchases electricity directly from a retailer this is considered to be a separate utility and the tenant contribution under the 'no worse off' pathway can be calculated based on the savings to that utility.

## SEMI-GROSS LEASE

A 'semi-gross' lease means that some operating costs/outgoings are passed through to tenants, but not all of them. The actual costs that are passed through will vary from lease to lease, and may even vary within a building. In this situation, the landlord can only recover a contribution from the tenant if the tenant is paying for the service that is upgraded.

For example, if the upgrade results in energy savings, and the landlord passes energy bills through to the tenant under the semi-gross lease, the tenant may be required to pay a contribution to the Building Upgrade Charge as long as the contribution does not exceed the savings to the tenant. If the landlord doesn't pass through the energy bills, the tenant can't be required to pay a contribution.

Under the 'no worse off' methodology, the calculations are determined for each individual tenant. If a building has a mix of tenants on net, gross or semi-gross leases, the individual lease agreements with each tenant determine the applicable tenant contributions.

## 13. How does the consent pathway apply to different types of leases?

Under the 'consent' pathway, the tenant and building owner may negotiate a contribution to the upgrade cost from the tenant regardless of the type of lease arrangement.

## 14. How are demand charges treated in the Methodology?

Some electricity customers have 'demand charges' included into their electricity bills. This demand charge is based on the maximum annual demand from the premises and is calculated in \$/kVA. Reducing the maximum annual demand for the premises will reduce the total cost of electricity bills for these customers.

Savings from reduced maximum demand are difficult to accurately estimate in advance and to measure. In the absence of an accepted and widely adopted method to estimate demand savings, the Building Upgrade Finance 'no worse off' methodology does not allow for inclusion of demand charges in the savings estimate.

Most building upgrade projects that reduce maximum demand are also likely to reduce overall electricity consumption in the building. Savings from reduced electricity use may be estimated using the Building Upgrade Finance 'no worse off' methodology.

## 15. How does the Methodology apply when there is a direct contract between the tenant and a utility supplier?

The Methodology may be used to calculate tenant contributions towards a Building Upgrade Charge when the utility is normally paid for by the tenant, whether through a direct contract with the utility provider or to the building owner through the provisions of the lease. See section 5.3 of the [Guide to the Methodology](#) for further details. The building owner should obtain and keep a copy of the relevant utility bills from the tenant to calculate the reasonable estimate of cost savings made by the tenant as a result of the building upgrade.

## 16. What is the dispute resolution process between a tenant and a building owner in relation to tenant contributions?

Existing arrangements to dispute resolutions between tenants and landlords apply. This means that for tenancies under the *Retail and Commercial Leases Act 1995*, dispute resolution provisions under this Act apply and a tenant may apply to the Small Business Commissioner for mediation.

*For further information about the use of the government-approved 'No Worse off' Methodology refer to [Department for Environment and Water website](#).*

*For Further information about Building Upgrade Finance visit [www.buildingupgradefinance.net.au](http://www.buildingupgradefinance.net.au)*

NOTE: This document has been prepared as a guide for potential parties to a Building Upgrade Agreement to assist in their understanding of some aspects of the Building Upgrade Agreement mechanism. It does not contain and should not be construed as legal advice. Any person or entity considering entering into a Building Upgrade Agreement should seek their own independent advice.