



European Bank
for Reconstruction and Development

Sub-sectoral Environmental and Social Guidelines: Leasing of Property and Land

PROCESS DESCRIPTION

There is a wide range of types of property and land holdings that can potentially be leased. Leased properties and landholdings may include private residences, public buildings (such as hospitals, schools and churches), industrial facilities and land, which may be used for agricultural, leisure, industrial, waste disposal, development, conservation and mining purposes.

Many of the environmental and social issues associated with the specific activities on leased properties are addressed in other subsector guidelines.

The purpose of this guideline is to outline the environmental and social risks associated with the general process of leasing property and land. The risks are primarily associated with the terms of the leasehold contract and the activities of the tenant.

Companies which specialise in leasing property and land often have large portfolios of sites and are continually acquiring and selling sites. Businesses need to carefully consider the risks associated with acquiring sites potentially contaminated from past or current uses, sites which are prone to contamination from neighbouring activities, which may pose significant social risks to the surrounding community, and those which are located in highly sensitive areas with limited commercial use (eg conservation areas, protected buildings etc.).

Leasing companies face a range of environmental and social risks, which could affect reputation, financial assets, links to the community and social and regulatory licence to operate.

The asset value of the whole leasing company can be significantly affected by the environmental status and social issues associated with the properties which are owned by the company.

Social issues affect the reputation of the company, relationships with local communities and moral licence to operate.

Well managed companies should have detailed records of material environmental and social issues associated with the leased site. These records should include information on major accidents, ground contamination (actual and potential), protection status (e.g. conservation areas, protected historical buildings) and the condition of the buildings prior to lease.

KEY ENVIRONMENTAL, HEALTH AND SAFETY RISKS/LIABILITY ISSUES

Contractual Arrangements

The contract between the leasing company and lessee should clearly define the responsibilities of each party. The lease agreement should refer to the relevant national and local legislation and should specify the legal obligations of each party.

Examples of environmental and health and safety issues that should be addressed include; on-site spills, housekeeping, employee accidents, surface water and groundmass contamination, damage or alteration to property, drainage, nuisance issues (odours, noise), prohibited activities on-site, record of complaints from neighbours or community groups and use/storage of hazardous materials.

Climate Change Adaptation

Climate change is widely regarded as one of the greatest challenges facing the world today. The scientific community now has broad consensus on the role human society has played in accelerating climate change through the release of greenhouse gasses associated with activities such as burning fossil fuels and deforestation. This has led to growing action on and expectations for climate change mitigation and adaptation.

Companies across industrial sectors face climate change related physical, regulatory and market risks. The real estate sector is vulnerable due to the impact of climate change on global weather



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patterns and temperature changes. Some regions of the world are expected to face rising sea levels, others increasing frequencies of drought and storms. These factors will affect the value of real estate and the construction requirements to adapt to different climate change risks.

Mitigation and adaptation efforts are already starting with regulatory efforts around building energy efficiency and greener construction standards. Commercial and residential buildings account for approximately one-third of greenhouse gas emissions worldwide. The European Union has already set directives for building energy efficiency for its member states. Over time, similar regulatory measures are likely to be enacted in other jurisdictions.

Climate related risks are also increasingly featuring in market decisions. For example, some properties with high geographical risks associated with climate change, such as floods or reduced agricultural productivity, may be less attractive to potential lessees and insurers.

Regulatory responses to climate change adaptation and mitigation are accelerating, exposing slowly adapting companies to higher compliance costs. There is a strong market and regulatory focus on green buildings and raising building standards to become more energy efficient and adapt to climate change impacts. In the UK for example, the government has imposed a zero-energy mandate for all new buildings starting in 2016. Property and land leasing companies should review their portfolios for risks related to climate change and make necessary property adjustments or asset changes.

Forward thinking companies are increasing building standards, retrofitting old buildings and saving long-term energy costs through energy efficiency measures.

Contaminated Land

Contaminated land is a significant risk for companies involved in the leasing of property or land. The leasing company may own contaminated sites that will be subject to clean

up, thus substantially reducing the asset value of the company. Alternatively the leasing company may have tenants, which have contaminated the company's property.

While some legal jurisdictions may operate under the 'polluter pays principle', in practice this is difficult to enforce and it can be the owner of the land that is ultimately responsible for any contamination that occurs, particularly where the original polluter cannot be found or has ceased to trade.

Pollution and Waste

All types of properties regularly generate waste through their operations. Waste management systems should be based on the potential environmental, health and safety risks specific to the activities of the leased property. Waste management plans and systems should exist as part of the sites' operational plans and be maintained by either the lessee or the leasing company depending on the lease agreement.

Failure to manage these risks can lead to environmental and social consequences (such as land contamination and human health impacts) and affect communities and industries downstream. Property owners may be held accountable through civil action or fines and penalties. Asset value may also decline due to contamination and property damage.

Occupational Health and Safety

Where leasing companies are responsible for the maintenance of their properties, they should have appropriate occupational health and safety policies and measures.

Where property maintenance is the responsibility of the lessee, the leasing contract should specify the expectation of achieving and maintaining appropriate standards for occupational health and safety.

Property companies and lessees commonly contract parts of property maintenance or



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construction to third parties. Contracts with third parties should specify compliance with national standards with respect to illegal labour, child or forced labour as well as environmental and occupational health and safety standards.

OTHER ENVIRONMENTAL, HEALTH & SAFETY RISKS/LIABILITY ISSUES

Site Sensitivity

Each site that is leased will have a different level of environmental sensitivity. This is based on factors such as site history, local hydrology, hydrogeology, and the existence of conservation areas (buildings and natural habitats), historic properties or sites of archaeological interest.

The leasing company should carry out an assessment of the environmental sensitivity of the site, and ensure that the operations carried out are compatible with the sensitivity of the site.

Damage to, or alteration of, existing properties may be illegal if the property or site is protected by legislation. Similarly, damage to persons or property may result in civil action and possible need for financial compensation.

KEY SOCIAL, LABOUR AND COMMUNITY RISK/LIABILITY ISSUES

Building Safety

Property leasing companies are likely to be responsible for ensuring the safety of the buildings they own and lease. This includes having sufficient air quality and ventilation, safe wiring and electrical components, and the use of safe materials in building construction and maintenance. Property owners are also generally responsible for the construction and maintenance of protective infrastructure built into the buildings. This relates to equipment such as cages and lifts for window cleaners and netting and railings on building roofs. Leasing companies should ensure that only authorised individuals have access to potentially dangerous features and areas such as exposed electrical wiring, boiler rooms or high voltage areas.

Buildings that contain asbestos for example, may be higher risk investments due to the substance's impact on human health through asbestosis or mesothelioma. Asbestos was widely used in older buildings as a fire proofing and insulating material.

Property owners are generally responsible for the fire safety infrastructure in a building. Specific requirements vary by jurisdiction and type of property but generally include the provision of emergency exits, fire detectors and alarm systems. Regulations may also require owners to include features such as fire escapes emergency lighting, fire extinguishers, fire hoses, fire alarms, smoke detectors, fire resistant doors and sprinkler systems. Industrial properties have additional fire protection requirements based on the type of facility.

Poorly constructed and maintained buildings have led to injury and death.

Corruption and Bribery

The real estate and property development sectors are characterised by high incidences of corruption and bribery. This has resulted in loss of human life where corrupt practices allowed poor building standards to be maintained. Companies face reputation and legal risks where neglect of sound environmental and safety practices and standards, as a result of corruption, lead to environmental damage or injury and death.

Corruption and bribery practices are illegal in themselves and companies also face the risk of financial penalties and fines along with the loss of business licences and permits.

Anti-corruption and bribery policies as well as whistle-blowing procedures should be in place. Where the leasing company contracts to third parties in construction or building maintenance, clear anti-corruption and bribery clauses should be maintained as part of the contractual agreement.



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Land Rights

Land rights and land claims are contentious issues related to issues such as historical land use by local groups or tribes, unfair land purchase practices, and involuntary displacement of people and communities.

Prior to acquisition, property companies should evaluate existing land claims and the legal standing of the property they are acquiring.

Companies should seriously consider the impact of acquiring land and property connected with the involuntary displacement of people and communities. Where this is unavoidable, appropriate re-settlement and compensation arrangements should be made towards the affected parties.

Companies should also consider the environmental and social impact of the property's intended use on the surrounding community and environment. Failure to consider these aspects can result in reputational issues stemming from NGO and stakeholder campaigns, as well as legal challenges and loss of property asset value.

OTHER SOCIAL, LABOUR AND COMMUNITY RISKS/LIABILITY ISSUES

Labour Standards

Labour standards are rules that govern working conditions and industrial relations. They may be formal, such as national level regulation and international agreements, or informal, expressed through norms and values. In general, developed countries have more robust labour standards than developing countries where the associated risks are higher. The commonly accepted rights and principles, enshrined in the International Labour Organisation standards, are the right to collective bargaining, elimination of forced or compulsory labour, abolition of child labour and elimination of all forms of discrimination. In addition fair wages and working hours, treatment

with respect and acceptable working conditions should be expected.

The leasing company is directly responsible for the labour standards of its own employees. Third-party contractors may be engaged to perform property or land maintenance works, construction, or janitorial duties. Ultimate responsibility for third party contracts on leased property may be lie with the property leasing company.

In such an event, the leasing company should ensure their contractors maintain appropriate labour standards in addition to sound health and safety practices. These include measures against forced, illegal or child labour and the provision of safe and fair working conditions. Leasing companies face reputational risks if their lessees do not do the same.

Supply Chain

The supply chain impacts of the leased site may be quite significant with respect to environmental and/or social issues. Supply chain risks may include issues such as illegally sourced wood in construction, poor labour standards in the supply chain, and over-exploitation of natural resources. Issues in the supply chain may be of greater concern than the direct risks and impact of the property itself.

Customers leasing properties and land may be bound by procurement policies that require their suppliers to have sound environmental and social policies and practices. For example, a lessee may require the leasing company to have appropriate working conditions for the maintenance staff of the leased property.

Leasing companies can also face business disruptions through poorly managed supply chains. Where their suppliers do not incorporate environmental and social risks into their operations, they may be unable to effectively conduct business. Examples include business disruptions from labour issues and loss of licence due to environmental damage.



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FINANCIAL IMPLICATIONS

Regulatory Risks

Companies may lose regulatory licences/permits if found to be negligent or failing to meet environmental and health and safety standards. They may also face fines or penalties.

Companies, which are slow to adapt to changing regulation also face compliance costs associated with increasingly stringent regulations with respect to environmental and social standards.

Litigation

Failure to clearly outline responsibilities in the leasing agreement, failure to meet regulatory or legal obligations, and/or negligence causing harm can result in litigation. This may be brought by individuals, communities, customers or government and can significantly reduce the asset value of a company.

Remediation

Site contamination may result in leasing companies being held responsible for costly site clean-up. Businesses should conduct pre-acquisition environmental impact assessments to avoid unforeseen liabilities and costs.

IMPROVEMENTS

The environmental, health and safety improvements needed at a given property or land will depend on the site location, country, surrounding environmental sensitivity, and the type of operations and activities conducted on site.

The responsibility for operation-specific improvements may or may not fall on the leasing company. The following improvements apply to the leasing company itself.

Environmental, Health & Safety Improvements

- Conduct pre-acquisition environmental impact assessments to identify environmental issues related to the property, such as contamination, pollution, high ecological sensitivity, presence of protected or endangered species, etc.
- Specify minimum environment, health and safety procedures and standards the lessee is required to follow in the leasing agreement.
- Regular review of property portfolio for environmental upgrades and maintenance improvements required.
- Regular review of tenant activities to ensure that there is no contravention of the lease agreement (e.g. high risk activities, unpermitted pollution).
- Review the property portfolio for necessary building improvements and energy efficiency upgrades in line with or ahead of legislative requirements. Consider certification schemes such as BREEAM.
- Where asbestos is present, obtain and record detailed information on the condition of the property and develop an asbestos management plan setting out how exposure will be prevented. Remove the asbestos, using licensed contractors, where necessary/feasible.
- Implementation and review of occupational health and safety standards and procedures for building maintenance staff.

Social, Labour and Community Improvements

- Consult the local community prior to major construction, land conversion or other activities that may impact community quality of life and environment.
- Include minimum labour standards for all third-party contractors working on-site. These standards should include provisions related to illegal, child and forced labour.



GUIDE TO INITIAL DUE DILIGENCE SITE VISITS

The issues and risks associated with a site will vary depending on the operations conducted on-site, the size of the property, the site location, the country of operation and the quality of management.

Risks related to the operations carried out on site vary significantly and are best assessed using the Guidelines specific to those activities.

When assessing a leasing company, some questions that should be considered include:

Environmental, Health & Safety

- What was the site used for prior to acquisition by the leasing company? This may reveal material environmental or social issues to be considered by the current management. For example, if the site was previously used by heavy industry, the property may be contaminated.
- Has the leasing company conducted pre-acquisition environmental and social impact assessments for all its sites? If these are available, review them for any significant issues and follow up on progress by the company on any recommended actions.
- Does the leasing company have valid permits and licenses to lease its properties?
- Does the leasing company have appropriate property insurance, including coverage of climate related risks where relevant?
- Have there been material incidents or stakeholder protests at or against any of the portfolio sites or the leasing company? How has the leasing company and/or its lesser addressed these issues?

- Are there any outstanding environmental, health and safety fines or penalties in the leasing company's property portfolio?
- Discuss terms in the contract relating to environment, health and safety issues.
- Discuss environmental, health and safety information available for each of the properties leased.
- Discuss how environmental liabilities at the sites owned could affect the asset value of the company and what further information is required to accurately determine the value of the property portfolio.
- Does the leasing company have Environment, Health and Safety policies and/or plans to make improvements to these areas in its business plan?
- Have the portfolio sites been inspected recently (within the past 2 years) by the regulatory authorities for health, safety and environment?

When visiting a portfolio site, consider the following:

- Check for signs of ground contamination from chemicals stored and used at the site, for example looking for stained earth/concrete, dead vegetation near storage containers and production areas, the integrity, condition and age of storage tanks and assess the age and integrity of the drainage system;
- What is the standard of housekeeping on the portfolio site? Do areas look clean and tidy? Look for evidence that the walking and working surfaces are kept clean and dry
- Check signage around the site. Does it convey the health & safety risks? Are the fire exits clearly marked?

Social, Labour and Community



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- Check that the leasing company's labour standards, contracting and remuneration are in line with national law and are consistent with the average for the sector.
- Check that the leasing company's working conditions are of adequate quality – working areas not cramped, access to drinking water, areas well lit.
- Check that the leasing company's hours worked, including overtime, are recorded and staff should receive written details of hours worked and payment received.
- Check that there are no illegal labour practices such as child or forced labour, prevention of the right to collective bargaining, discrimination (by interviewing a sample of the workers if possible).
- Check that the leasing company has a policy against bribery, corruption and a whistle-blowing policy.
- Check whether the leasing company has a business code of conduct.
- Has the leasing company received inspections from the local labour inspectorate in the previous three years? Have these resulted in any penalties, fines, major recommendations or corrective action plans?
- Does the leasing company have a grievance mechanism which allows employees to raise workplace concerns?
- Are employees of the leasing company free to form, or join, a worker's organisation of their choosing?
- Conduct a press scan to gain an understanding of the nature of media coverage surrounding the leasing company.

A property leasing company should develop action plans based on the risks and types of property and land it owns. Recommended environmental and social actions or policies include:

Environmental, Health & Safety

- Conduct pre-acquisition and divestiture audits on all property holdings.
- Maintain accurate and comprehensive information on the environmental status of all properties owned.
- Ensure compatibility between the site sensitivity and proposed operations.
- Regular review of leasing contracts in terms of environment, health and safety risks.

Ensure properties are maintained in a good state of repair, and that land holdings are managed in compliance with the national legislation on conservation and land management issues

- Assess properties and land holdings for environmental damage prior to releasing the lessee from the contract.

Social, Labour and Community

- Develop or improve labour standards for own and third-party employees or contractors to at minimum be in line with national regulations.
- Review the lessee's intended use of the property or land and whether the company faces material unresolved environmental or social issues. Consider these factors in deciding to lease products to such businesses.

ACTION PLAN



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REFERENCES AND ADDITIONAL SOURCES

BREEAM - <http://www.breeam.org/>

European Commission – Energy - http://ec.europa.eu/energy/efficiency/buildings_en.htm

Inter-governmental Panel on Climate Change - <http://www.ipcc.ch/>

International Labour Organisation - <http://www.ilo.org/global/lang--en/index.htm>

Transparency International - <http://www.transparency.org/>

World Business Council for Sustainable Development – Energy Efficiency in Buildings -
<http://www.wbcsd.org/Plugins/DocSearch/details.asp?DocTypeId=251&ObjectId=MjYyODg>