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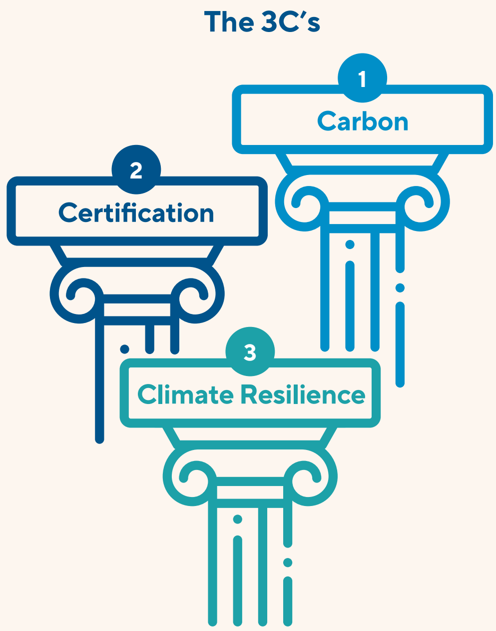
The 3C's of ESG in Real Estate

Discover how to set a strong foundation for your ESG strategy with these 3 pillars

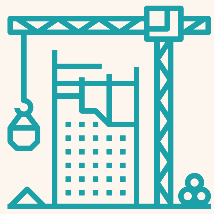
Introduction

ESG is seriously lacking structure. This may not be ground-breaking news, but frustrations are not tempering any time soon. In the real estate sector specifically, a place where scrutiny is feverishly increasing, there is a real lack of consensus as to what an ESG integrated portfolio actually looks like. Sustainability strategies are stagnating, targets are not being met and there's no uniformed approach to benchmarking as everyone is doing their own thing. That's not to criticise organisations' best intentions but without a uniformed approach to ESG, only confusion and apprehension will continue to remain. Therefore, we outline 3 fundamental pillars to ESG that will sustain your strategy and provide greater clarity and cohesion in the real estate market: Carbon, Certification and Climate Resilience. 3C's to ESG is not an extensive account of everything that is needed, however this will help create a collective approach to reporting on environmental mitigation and adaptation in the real estate sector.



3C's of ESG:
Carbon

Carbon reduction will be at the centre of your ESG sustainability strategy in regard to the scope and focus. An increasing number of organisations are including their commitments to carbon reduction in their ESG plans as it is an achievable and measurable way to have more of a positive environmental impact at scale. Yet, while many organisations have adopted carbon reduction into their strategies, there is persistent failure to sufficiently address the core issues of carbon which has exacerbated rather than resolved the problem of climate change. Multiple factors explain this failure: incomplete measurements, inconsistent data reporting, and poorly informed decision making. Compounding the problem is also a skewed emphasis on operational rather than embodied carbon.



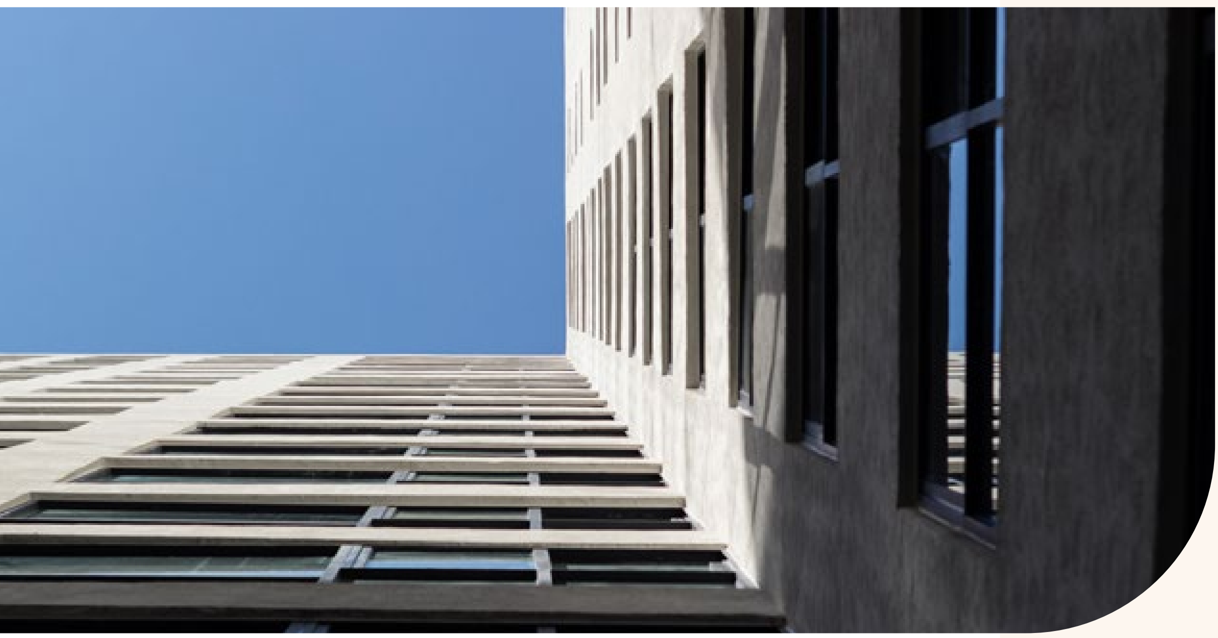
Stakeholders need to pay attention to the **whole life cycle of buildings**, from the construction phase right to the end-of-life stage

Real Carbon Reduction

It's first important to consider what real carbon reduction looks like in the real estate sector. Stakeholders need to pay attention to the whole life cycle of buildings, from the construction phase right to the end-of-life stage when they are demolished. Actively partaking in, and contributing to the circular economy is absolutely crucial to hitting the targets needed to curb the industry's emissions in line with the goals of The Paris Agreement. Construction, maintenance and ongoing energy consumption comprise most of the real estate sector's carbon emissions and so understanding all types of carbon emissions from a building will help you address the question of how you can measure them. Only once this is fully understood can you start to consider how you will report your data and integrate your findings into your ESG strategy.

Embodied and Operational Carbon Complexities

Operational carbon has been a longstanding focal point of sustainability strategies in the built environment. This makes sense, since two thirds of global carbon emissions from buildings are due to operational carbon and it is also the easiest out of the two to deliver results. While there have been innovative leaps and bounds achieved for maximising energy efficiency in the daily operations of a building, there is a serious lag in translating this efficiency to another key component of a building's carbon lifecycle: embodied carbon. This is mainly due to the extensive range of challenges associated with this stage.



However, if you don't have an embodied carbon strategy, you don't have a carbon strategy at all. It is going to be an increasingly important focal point in new builds and there has been no greater time than now to make more informed material choices for buildings. Regulatory bodies such as the Greater London Authority (GLA) and BREEAM have integrated their recognition of this into their updated criteria that enables a wider snapshot of a building's sustainability potential. With this shift in focus towards embodied carbon, and an emphasis on enhancing the life cycle outputs of core assets, there will need to be transformative change in the baseline business-as-usual scenario. This is so that building assets used from the construction phase right through to how demolished building materials can be reused in future projects. When done right, this can have a positive impact on your real estate portfolio and present a huge opportunity for your ESG strategies going forward.

Unifying Your Data

The only way we can make progress on reducing operational and embodied carbon is if we have the right data. Unfortunately, accurate data measurement and reporting is not only a pain point in the real estate sector but across a wide range of industries when it comes to sustainability. Over the past few years there has been significant growing pains in terms of reporting regulations playing catch-up. Whether it's the lack of clarity on the likes of Scope 3 and how far we should cast our net, or the lack of EPDs and material insights available, it's no wonder organisations are scrambling around for greater detail.

However, with the likes of third-party certification like Natural Carbon Solutions there is an opportunity to verify and certify your carbon reduction actions. Providing such consistency is going to be vital to delivering credible data reporting which will help create a more unified carbon reduction approach across the industry, and in turn better benchmarking opportunities for your ESG plans. It's crucial to employ certification standards that yield higher data resolution so that you can make more informed reduction decisions for both operational and embodied carbon. If stakeholders such as suppliers and manufacturers follow better standards of data measurement and reporting, 'the data gap' will lessen and the generic, inaccurate data currently being used in ESG reporting will be a thing of the past.

Be Resourceful

If you don't have a comprehensive carbon measurement and reduction plan, you don't have an ESG strategy. Yes, the data is challenging and not where we need it to be, but the first step is being resourceful and maximising what you have. By asking the right questions and investigating what's needed you can ignite behavioural change that will ripple through to your supply chains. Your ESG strategy can be more measurable, impactful, scalable and even benchmarkable with your carbon plans which can not only transform your organisation, but also the industry as a whole. Being resourceful and demanding more from all stakeholders is what's going to make the difference. With enough tools and solutions already in place for reducing carbon, it is simply a matter of when, and not if, real estate companies should get started.

> "If you don't have an **embodied carbon strategy**, you don't have a carbon strategy at all."

3Cs of ESG:

Certification

Certification in real estate ESG means assessing your building's sustainability performance against core criteria that follow a holistic approach that is driven by data. Following a reputable certification scheme helps you mitigate risks of greenwashing whilst allowing you to benchmark your performance and identify areas to improve. In today's landscape where governments are introducing new laws that require companies' full disclosure on environmental data, certifying your buildings is more crucial than ever. Yet finding the right certification scheme to apply to your building or project is not a simple process.

Following a reputable certification scheme helps you mitigate risks of greenwashing

Types of Certifications

Your sustainability claims won't hold up if they are not backed by a certification body. To mitigate the question of transparency, there are a number of certifications that you can obtain to prove your claims. We recommend considering BREEAM, WELL, Carbon and GRESB schemes which allow you to hone your strategy in line with a holistic and data-driven approach. Each scheme has a variety of benefits and requires you to undertake an extensive audit of your building or project:

BREEAM

BREEAM is one of the most popular and broadest certification systems for buildings in the UK. In 2019, BREEAM In-Use was developed to comply with major regulatory requirements as well as adapt to future changes. Doubling as an assessment and certification scheme, BREEAM In-Use can be applied to all building types. It aids building owners, investment managers and facility managers in measuring and reducing environmental impact and enhancing the performance of non-domestic buildings.

BREEAM helps pave the way for planning approval and is actually a mandatory requirement for many London-based Local Planning Authorities (LPAs). It enables you to validate your disclosures and reporting, as well as whole life performance, health and social impact, and circularity and resilience which can be applied to new builds or in-use buildings. Because BREEAM is third-party verified, it provides ESG-grade data that can also yield huge potential value for asset managers.

WELL

With an emphasis on occupant health, WELL certification is the gold standard of auditing your building's performance for both the 'E' and 'S' in your ESG strategy. WELL looks at 7 "concepts" of a building's impact on occupant health: air, water, nourishment, light, fitness, comfort and mind. The current WELL system is optimised for commercial and institutional office buildings and can be applied to three project types: new and existing builds, new and existing interiors, and core and shell models. Asset managers in particular should be striving to implement a WELL strategy to maximise tentants' productivity and health gains. The positive results from this scheme are another way to demonstrate third-party verification of your ESG initiatives.

WELL

Carbon

As mentioned, carbon is a critical element to include in any ESG strategy. Without measuring and reducing your carbon emissions, you simply don't have a strategy. Given that it is measurable, many buildings have already started to reduce their carbon emissions for both operational and embodied carbon. Achieving certification with each of these steps is an important part of any ESG strategy so that you can demonstrate the credible actions you are taking to achieving a Net Zero building. Natural Carbon Solutions is one of the first of its kind to offer a robust certification method that adheres to all of the highest industry standards which will play an integral role in the future of sustainable buildings.

Natural Carbon Solutions

GRESB

GRESB is not a certification scheme, but a global ESG benchmark that collects, validates and scores ESG data. The scheme is especially ideal for financial and asset assessment, as the data analyses caters to both investors and asset managers.

Catering specifically for ESG strategies by evaluating portfolios on a broader scale, GRESB can be a useful verification tool for those seeking to conduct analyses of multiple assets. This is particularly useful for real estate stakeholders as GRESB assesses levels of ESG disclosure alongside a comprehensive evaluation of management, development and performance components.

GRESB

Regulation Outlook

An ongoing problem in ESG reporting is that more often than not, data disclosure and performance standards are not aligned. Setting science-based targets is pivotal to bolstering your approach to environmental impact in your ESG strategy. This will enable you to pivot according to whichever crises arises so that you can revise your goals. The certification schemes mentioned are all designed to mitigate risks of greenwashing, data misalignment, failure to reach KPIs and financial loss.

These schemes also ensure you're complying with the current regulatory landscape that has started to include more rigid standards in the past year alone. The Sustainability Reporting Directive will be changing its name to the Corporate Sustainability Reporting Directive (CSRD) following amendments to its requirements. These updates are expected to be rolled out within the next two years. Major changes include:

- A wider number of companies will be required to provide ESG reporting adhering to EU standards (which have yet to be decided on)
- Content of the reports will be audited

The UK government has already begun implementing stricter reporting standards with two new regulations that have been made law as of April 2022:

- The Companies (Strategic Report) (Climate-related Financial Disclosure) Regulations 2022
- The Limited Liability Partnerships (Climate-related Financial Disclosures) Regulations 2022

Boost Your Visibility

The shifts we are seeing in real estate ESG are driven by regulation and technology to drive accountability and transparency. With that being said, it's only going to get more difficult to stay under the radar with your data disclosures and reporting. Certifying your strategy only serves to strengthen your ability to adapt and keep up with future regulations. Whether mandatory or voluntary, certification has its power within an ESG strategy. These schemes integrate forward-thinking data into your ESG plans that you can use to your advantage in areas that investors are becoming increasingly interested in. Being able to clearly demonstrate your portfolio of sustainable buildings via these certifications will boost your visibility in this space and create greater opportunities for those looking for greener investments.

3C's of ESG:

Climate Resilience

Climate resilience in the built environment has become an increasing concern for the market as the visibility around the hazards resulting from climate change have grown exponentially. Whether it be from floods, draughts, earthquakes or any other natural disasters associated with climate change, these shocks and stresses can undermine the stability of your assets and portfolio value. It will ultimately make or break your business if not dealt with appropriately as companies are already having to write off £millions from their portfolio due to stranded assets.

Across the board, the cost of adapting to climate change is estimated to be up to $500 billion per year in 2050 and an average of $2.5 trillion of the world's financial assets would be at risk from these impacts. Resilience is not just a valuable risk management mechanism, but there are many financial and operational benefits that help hold asset value in the medium to long term. It's no surprise then that the financial well-being of real estate companies will depend on the ability to introduce resilient practices to appease investors and banks who are crying out for it. Not to mention the increasing level of regulation in this area and the pressure to meet any Task Force on Climate-Related Financial Disclosure requirements (TCFD).

Cost of adapting to climate change up to **$500 billion per year in 2050**

A framework to help companies disclose climate-related risks and opportunities

TCFD

Stranded Assets

A key risk to be aware of within your existing building portfolio are stranded assets. Stranded assets are one of the most troublesome consequences of failing to integrate climate resilience into your building from the beginning. A nightmare in the investment world, stranded assets are those that have suffered unanticipated devaluations or conversion to liabilities. Factors that lead to stranded assets include changes to regulations, climate crises and changes to economy. Stranded assets are now wreaking havoc in the investment world as we shift to a lower-carbon economy. The oil and gas industries have been suffering greatly from stranded assets as behavioural demand shifts to higher energy efficiency and climate change impacts the feasibility of extracting fossil fuels.

Building Resilient Buildings

There are plenty of nuances to what can be included in a resilient building as it depends on many factors, but we consider how you can introduce climate resilience strategies for existing and new builds:

Existing Buildings

For an existing building, you need retrofitting adaption measures that focus on reducing the vulnerabilities and risks resulting from different climate change scenarios. These measures exist today, however the difficulty is how you deal with the constraints and trade-offs necessary to successfully adapt a building. It is also challenging to understand which climate risks are most likely to affect your building and therefore what mitigation measures need to be put in place. For example, where there is a high risk of flooding, you may be able to introduce Sustainable Drainage Systems (SuDs) to the surrounding area before you tackle any resilience measures within the building. SuDs is a highly effective method to introduce as it typically can manage rainfall more effectively and purposefully so that you reduce any flood risk to your buildings. Alternatively, where increased heatwaves and potential droughts are more likely, you could introduce external shading to reduce heat gains, better ventilation with higher flow rates, or consider upgrading the cladding and fabric of the building for greater thermal comfort during heatwaves.

Resilience from the Ground Up

Climate resilience strategies for new developments can be built from the ground up to mitigate risk. The necessary forward-thinking approach that confronts future risks and opportunities should be integrated into your building from the design stage. Innovation and knowledge on enhancing circularity and climate resilience in buildings is still growing, but there are a number of elements to consider when mitigating climate risk. For example:

STRUCTURE
Moisture can often impact the structure of buildings so structures need to consider humidity, wood rot and corrosion issues to mitigate long-term damage

INTERIORS
Heat and humidity will affect indoor climates so extra cooling capacity will be needed which will drive up electrical demand and increase operational cost

MASSING
Taller, more open buildings expose themselves to the natural elements which could leave your building vulnerable to more aggressive winds and storm events

MATERIALS
More durable materials will need to be considered to avoid the acceleration of deterioration due to climate change such as increased UV exposure

Long-Term Approach

Climate resilience can only be achieved when you convert the pledges you're making into meaningful action. Considering resilience either at the existing or new build stage can improve your portfolios performance and result in greater financial returns. When applying this long-term strategic approach to your assets, you can implement the necessary changes and display these to your stakeholders within your ESG reports. This means you'll be able to make more informed business decisions and meet any disclosure guidelines from the TCFD.

Summary

Eight Versa has been working with the built environment for over 14 years and have helped numerous clients build a more sustainable foundation for their ESG strategies. The 3C's of ESG are not meant to be exhaustive, but instead an introduction to what will help move the real estate market closer to a more uniformed approach to ESG.

We've seen how these 3 pillars can build greater improvements, cohesion and clarity but understand a well-structured ESG framework can incorporate much more. A strong ESG proposition links to value creation in many ways, from increasing revenue growth and reducing costs, to boosting employee motivation and enhancing investment returns. And this often requires a fundamental strategic shift in operations to implement successfully. That's why we support you throughout this process and help you build an ESG strategy that incorporates real purpose, incentivises and tracks meaningful behaviour, and is verified by independent third parties.

No one expects change overnight, but if you are considering where to start, or how to build on what's been implemented so far, get in touch with one of our ESG consultants and we'd be happy to help.

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