Agreement in Principle

Mr FRANK SARTOR (Rockdale—Minister for Climate Change and the Environment, and Minister Assisting the Minister for Health (Cancer)) [10.34 a.m.]: I move:

> That this bill be now agreed to in principle.

Improving energy efficiency in the building sector offers the most cost-effective greenhouse gas emission reduction opportunities of any sector in the economy. That is why I am introducing the Local Government Amendment (Environmental Upgrade Agreements) Bill 2010 as a climate change measure. However, improving energy efficiency in the building sector also makes good economic sense. Even if it did not reduce one tonne of greenhouse gas emissions this bill should be supported. The bill will directly help reduce the impact of growing power demand on our electricity network and the impact on power prices. I acknowledge the support and assistance I have received from the Minister for Local Government and I thank her and her department for their contribution to this legislation.

A recent report by the policy research body ClimateWorks using McKinsey and Company data found that investing in energy efficiency projects in commercial buildings would deliver a total potential benefit to the New South Wales economy of more than $560 million each year, and that rather than costing money to reduce carbon, each tonne of carbon reduced would be equivalent to a $100 benefit. However, these potential savings opportunities in commercial buildings are not being implemented at anywhere near the scale that the financial analysis shows they should be.

There are two major barriers to action and this bill provides a path through each. The first barrier is access to capital. Currently, building owners may be able to obtain a loan of around three years duration for an energy efficiency upgrade. This will allow the owner to implement some small to medium-sized projects, such as a lighting upgrade. But this type of loan is too short and potentially too small to implement larger projects which deliver the biggest savings. Unlocking the full energy efficiency potential in large buildings requires investment in more comprehensive measures, including upgrades to air conditioning, heating and ventilation, lighting, and building management systems.

Whilst the projects will vary, with some taking longer to implement, some having high upfront cost and others having longer payback periods, the projects that we want to see implemented are the ones that will lead to the greatest net energy and bill savings and environmental benefit. This bill enables the establishment of an innovative financing mechanism—environmental upgrade agreements—to assist building owners to gain access to commercial finance, potentially at lower cost and certainly at the scale and in the time frames needed to progress cost effective environmental upgrade works. The bill amends the Local Government Act to enable local councils to enter voluntarily into environmental upgrade agreements with a building owner and a finance provider to upgrade a building's environmental performance.

Under the agreement, the lender provides funds to the owner, who then upgrades the building. The owner then makes regular loan repayments to the local council in the form of a special rate or charge. Once the repayment has been received by the council, the council forwards it to the lender to repay the debt. The environmental upgrade agreement will specify what works are to be carried out, the amount of money to be provided in total and the repayment arrangements. Participation is completely voluntary. No building owner, council or lender would be required to participate. Officers of my department have, however, already received strong indications of support and interest from representatives of the property sector, the banks and leading local councils.

Buildings last for a long time but owners can come and go. Energy efficiency upgrades may be up to 10-year projects, which is longer than many businesses' usual investment horizons. Because the loan becomes a charge fixed to the land—which is very secure—rather than to the building owner's business, longer-term loans at lower interest rates can be provided. This brings me to the second barrier to energy efficiency that the bill will overcome. This is known in the industry as the split incentive between landlords and tenants. In leased properties the building owner makes the decisions about implementing energy efficiency upgrades, but the tenants would often receive the most benefits through lower power bills. Because the tenant pays the power bill there is little incentive for building owners to invest.

Environmental upgrade agreements can overcome this because most leases provide for proportional pass-through of local council rates and charges. In most agreements under this bill instead of paying a large power bill the tenant will pay for a smaller power bill and a contribution to repaying the costs of the upgrade works. Once the upgrade cost is repaid, the tenant will experience an ongoing benefit in the form of lower outgoings. The bill provides an important protection for tenants. It requires that no tenant can be required to pay more than they would had the agreement not been put in place, unless otherwise agreed by the tenant and the building owner. This ensures that tenants will not be disadvantaged as a result of environmental upgrade agreements. Overcoming the split incentive will, however, improve cash flow and return on investment for the building owner, which is also attractive to the lenders and will further support longer loan periods.

Tenants will benefit from the reduced electricity bills from energy efficiency upgrades that otherwise would have been unlikely to happen. The combination of the above benefits means that the finance provider can potentially offer building retrofit finance at a lower cost and with longer terms than other loans, enabling bigger projects with greater savings to be undertaken. As I want to emphasise, participation in environmental upgrade agreements by property owners, lending institutions and local councils is completely voluntary. Interested councils will be able to opt in to enable the use of the agreements within their area. It is expected that this will be of most interest to urban councils with large stocks of commercial or large multi-unit residential buildings within their area.

The bill allows councils that decide to participate to recover their administrative costs through a service charge on the participating building owner. Importantly, councils will not be liable for repayments in the event that a building owner does not make required repayments. If building owners do not make their repayments councils are required to make best endeavours on behalf of lenders to recover unpaid moneys, utilising the range of recovery options that is already available to councils in the Act. The Minister for Climate Change and the Environment, in consultation with local government and other stakeholders, will develop guidelines for the operation of the environmental upgrade agreements. This will include specific information on the calculation and recovery of contributions by tenants, arrangements for reporting on progress of agreements, prerequisites for councils to participate, template agreements and other procedures required for use.

In addition to the environmental benefits, this mechanism will help building owners and tenants reduce their electricity bills. The overall reduction in demand for electricity that will result from these upgrades will benefit the whole community. The commercial property sector in New South Wales consumes around 16,000 gigawatt hours of electricity annually, and this continues to grow. The growth in energy use has primarily resulted from growth in total square meters of commercial building space, growth in use of computing and other office equipment, changed behaviours, such as extended shopping hours, and increased service levels, such as greater use of air conditioning, lighting and electronic equipment of all kinds. Increased demand for electricity is one of the main drivers of recent price rises for electricity in New South Wales.

Electricity network infrastructure needs to be augmented to meet this increasing demand, pushing up prices. Thus, measures like the environmental upgrade agreements provided for in this bill that have the potential to significantly reduce demand for electricity will benefit the whole community, as a reduction in demand is ultimately a saving for all electricity consumers. The introduction of this bill is timely. On 1 November this year the Commonwealth Government's Commercial Building Disclosure Program commenced. Under the program, owners of office space of 2,000 square metres or more will be required to obtain and disclose an up-to-date National Australian Built Environment Rating System [NABERS] energy efficiency rating to their prospective buyers or tenants. NABERS is a national building rating tool developed by the New South Wales Government.

The purpose is to provide buyers and tenants with information on the energy performance of a building so that operating costs can be considered in purchasing or leasing decisions. By increasing awareness of the energy performance of buildings, this program is expected to help drive the market for greener buildings. Building owners with low energy performance ratings will be competing for tenants and buyers with buildings that perform better and are therefore cheaper to occupy. More buildings than ever will have a NABERS energy rating as a result of the new Commonwealth program. It follows that more buildings than ever will be interested in taking action to improve their energy performance. The establishment of environmental upgrade agreements will enable the owners of these buildings to take more action sooner to reduce their energy consumption.

The measure is doubly timely because the Commonwealth Government intends to commence additional tax benefits for building owners who upgrade their building's environmental performance from 1 July 2011. This proposal has been developed in consultation with the Local Government and Shires Associations and representatives of key local councils with large areas of commercial property, the property industry and banks with an interest in funding energy efficiency projects in commercial buildings. The consultations have been very constructive and have produced a bill with a workable and practical approach which balances the range of stakeholder interests. I have been advised that two banks have indicated support. The National Australia Bank indicated that this approach will assist the commercial sector unlock the market barriers that have traditionally held back investment in building retrofits.

One estimate for the sector is that new investment in the New South Wales property sector could exceed $2 billion. This measure was initially developed as part of the Government's ongoing efforts to promote the uptake of energy efficiency. However, this model can also be used for other kinds of environmental upgrades for buildings. As a result the bill defines "environmental upgrade works" as works to improve the energy, water or environmental efficiency or sustainability of a building. The bill also enables bodies corporate of large strata-titled residential buildings to participate if they so desire. The New South Wales Government leads the nation in its energy efficiency programs, with our $150-million, five-year strategy and our Energy Savings scheme with a legislated electricity consumption reduction target which will reach 4 per cent in 2014.

This new measure will build on this by specifically addressing the split incentive and access to finance barriers in commercial buildings. With this new legislation, New South Wales can look forward to substantial new investment in upgrading existing large buildings. This will generate significant new employment and activity in the construction sector over the next five years, substantial improvements in the economic performance of the State, reduced occupancy costs for tenants and reduced pressure on power bills for all customers over the next five to 10 years. I commend the bill to the House.