

# DECEMBER 9TH 2024 - MEETING SUMMARY

*Focused Meeting on Commercial Real Estate for BEPS*

*Zoom Call 2PM – 4PM*

**Present:** Ana Duffy, Anita Jeerage, Catherine Stanford, Daniel Poppe, Danny Bucher, Edmee Knight, Ian Goepferd, Jack McCullough, Jake Reid, Jake Gustafson, Jake Randolph, Jeremy McPherson, Joe Malaspino, Mark Astor, Riley Lynch, Rod Kauffman, Sabrina Villanueva, Scott Koppelman, Shawn Jackson, Steven Yi, Todd Sparrow, Tony Toppenberg.

**City of Seattle BEPS and Facilitation Staff:** Gemma Holt, Nicole Ballinger, Kyle Berbel and Michelle Caulfield (OSE), Anna Kelly, Catherine Ozols, Faith DeBolt, and Santiago Rodriguez-Anderson (SBW), Kirstin Pulles and Sepideh Rezania (Unrooz)

**Additional City of Seattle Staff:** Duane Jonlin (Dept of Construction & Inspections) and Irina Rasputnis (City Light)

**Meeting slides are posted at:** <https://www.seattle.gov/environment/climate-change/buildings-and-energy/building-emissions-performance-standard/beps-rulemaking>

## Agenda:

Topic	Time
Welcome + Introductions	10 mins
Review: Introduction to the BEPS Rulemaking Process	20 mins
Review: Flexibility measures in BEPS important to commercial real estate	10 mins
Breakout discussion: Extensions for high rental vacancy	30 mins
Review: Deduction for district energy (steam)	5 mins
Discussion: Compliance with private building portfolios	10 mins
Review: Custom decarbonization plans	5 mins
Open discussion	25 mins
Wrap-Up & Next Steps	5 mins

## Working Group Discussions Summary:

### 1. Introduction to the BEPS Rulemaking Process.

**Topic:** The BEPS ordinance was shaped by many stakeholders, including the HDC Affordable Housing Study and Task Force, a Technical Advisory Group, building owners, residential and small business tenants, labor and trades, and public open houses.

The policy was developed in 2022 and 2023 with program development through 2026. The Director's Rule is currently in development and will be published by mid-2025. The rulemaking process includes a facilitated Technical Rulemaking Workgroup, focused topical meetings on key topics, and public webinars. The rules will also be updated periodically with stakeholder engagement through 2044, including GHGITs, emissions factors, and penalty amounts.

In 2027-2030, Benchmarking Verification and a GHG Report will be required while building owners begin planning for emissions reductions. Beginning in 2031, building owners will move through multiple compliance cycles. Every five years, building owners will need to verify the building's energy use (Benchmarking Verification), submit a GHG Report, and meet a Greenhouse Gas Intensity Target (GHGIT).

OSE recognizes that buildings in downtown Seattle are experiencing significant challenges with occupancy.

Building owners have three pathways available to them for BEPS compliance. Path A is to meet the Standard GHGIT or building portfolio/campus GHGIT in all five-year compliance intervals. Path B is to receive either an extension or alternate compliance through the Alternative Compliance Payments (ACP), the multifamily prescriptive path, or an Alternate GHGIT (a custom percentage reduction target). Path C is to follow a custom timeline and/or target due to hardship or unique circumstances via a net-zero or low-emissions decarbonization compliance plan. Path C also includes district campus decarbonization plans.

The Rulemaking goals, process, and timeline for the first Director's Rule, and subsequent Rule updates were also shared.

#### **Discussion:**

An attendee asked whether emission factors could change before the first compliance cycle. OSE explained that the ordinance sets provisional emissions factors for 2031-2035, with the goal of updating them by December 2027 to provide sufficient time and certainty for planning the first compliance cycle. Another attendee raised concerns about fines for non-compliance, describing them as excessively high and potentially problematic, and inquired about the relationship between flexibility and fines. OSE clarified that the intent of flexible compliance paths is to support planning efforts to avoid

non-compliance. When asked if the director has the flexibility to adjust the timing and application of fines, OSE responded that some flexibility exists, particularly if a building is close to meeting its target and noted that pathways like the decarbonization plan allow for alternative compliance timelines.

## 2. Extensions available in BEPS important to commercial real estate.

**Topic:** There are two BEPS extensions that are most relevant to commercial real estate.

**Financial Distress** – The ordinance (SMC 22.925.020) states that “Covered buildings under pre-existing financial distress at their compliance date may receive an extension from meeting the requirements of this Chapter 22.925 for each compliance interval they remain under financial distress.”

In order to qualify, building owners must document one of the following pre-existing conditions.

1. Building has had **arrears of property taxes** or water or wastewater charges that resulted in the building’s inclusion, within the prior two years, on a King County annual tax lien sale list;
2. Building has a **court-appointed receiver** in control of the asset;
3. Building is owned by a financial institution through **default by a borrower**;
4. Building has been acquired by a **deed in lieu of foreclosure** within the previous 24 months;
5. Building has a senior mortgage subject to a **notice of default**; or
6. Other conditions determined by rule.

**High Rental Vacancy** – The ordinance (SMC 22.925.020) states that “A covered building with a high rental vacancy rate, as determined by rule, during a consecutive 12-month period within the 36-months preceding the relevant compliance date may receive an extension from meeting the GHGIT for one compliance interval. Building owners must still meet benchmarking verification and all reporting obligations.”

OSE is considering defining vacancy in the following ways:

- Physically vacant space isn't be leased, doesn't have equipment for tenant/business needs (except for showing), and the lighting and mechanical systems may be shut down
- Space in the building considered “common space (lobby, parking, elevator, etc.), mechanical space, space reserved for the owner, or space that is leased but not occupied can't be included in the calculation of vacant space
- Spaces in buildings where tenants primarily work from home are not considered vacant

OSE worked with consultants from Community Attributes Inc. to get CoStar data about

rental vacancies. The findings confirmed what OSE heard from stakeholders about market conditions: office vacancy remains high (17.1% as of Q1 2024).

There is precedent in the Building Tune-ups requirement for allowing extensions for high rental vacancy. To apply for this extension, building owners must submit:

- Total gross floor area (GFA) excluding parking
- Total vacant nonresidential GFA
- Vacancy starting date and ending date
- Short summary of the reason(s) for the vacancy

### **Discussion:**

An attendee asked whether exemptions in the ordinance, such as those for significant new electrical infrastructure, would be discussed during the meeting. OSE explained that significant infrastructure upgrades are one of the circumstances that allow for pursuing the decarbonization compliance plan path. They acknowledged the complexity of these issues and noted that they have not yet begun to frame them fully but plan to introduce them later in the discussion and revisit specifics with relevant stakeholders. Another attendee suggested that Seattle City Light (SCL) and the Seattle Department of Construction and Inspections (SDCI) establish dedicated compliance teams, emphasizing that interfacing with these departments regarding BEPS could otherwise be challenging.

### **3. Extensions for high rental vacancy.**

**Topic:** OSE asked whether there were any issues or additional context needed for defining rental vacancy.

OSE also asked what vacancy/leasing trends attendees were seeing, what sources of information they use to learn about leasing trends and outlooks, whether different building types were experiencing different vacancy rates and outlooks, and the relationship between vacancy rates and financial constraints on buildings.

Attendees were asked what percent (%) vacancy should be set in the BEPS Director's Rule to allow an extension for high rental vacancy.

Finally, OSE asked the attendees what other documentation, such as lease rolls, photos, or verification in CoStar, could be used to demonstrate eligibility for a high rental vacancy extension.

### **Breakout Room A Discussion:**

An attendee noted that when leases come up, most tenants are downgrading or terminating, citing factors like work-from-home trends, safety concerns downtown, violence, and theft. They mentioned that while tours of buildings are increasing, more tenants are still being lost than gained. Another attendee stated that significant change

is not expected in the next year or two, with Class A office buildings, biotech, and industrial sectors performing better than others.

Another attendee pointed out that lower vacancy rates limit cash flow, leading owners to delay or cancel projects, with limited capital being reserved for tenant improvements. High interest rates were cited as a major barrier, with lenders less flexible in extending credit, leaving many owners struggling just to maintain ownership.

Several attendees suggested the vacancy rate was around 30%. A recent article in The Seattle Times was referenced for details on the vacancy rate.

An attendee shared that leasing velocity is low, tenant sizes are small, and the market feels very competitive. They observed that small tenants prefer more amenities but are unwilling to invest in building them out, while contractor rates remain high. Kirstin Pulles asked whether attendees expect these challenges to persist long-term, receiving mixed responses.

Discussion of poll results followed, with attendees estimating that a 30-40% vacancy rate is when buildings become unable to cover expenses and generate some operating revenue. It was noted that costs can be passed to tenants, but with fewer tenants, the financial burden is higher. However, attendees also noted that coming up with one set number is challenging. Building age and ownership timing were identified as factors influencing financial stress, with older buildings described as “capital hogs” due to numerous legislative mandates. Attendees emphasized the importance of understanding upcoming capital expenses, such as seismic retrofits, from a broader perspective.

The conversation shifted to tools like CoStar as a way to prove vacancy rates, which was noted to be expensive for smaller operations, potentially presenting an equity issue. Rent rolls were suggested as an easier and more commonly used alternative, though confidentiality was highlighted as a priority for sharing such data.

### **Breakout Room B Discussion:**

In the discussion about defining vacancy rates, an attendee raised the issue of tenants in default who are not paying rent, despite technically leasing the space. Another attendee explained that vacancy is often used as a proxy for financial performance, encompassing direct vacancy, shadow or sublease vacancy, and other scenarios. They pointed out that space could be leased at significantly reduced rates to attract tenants, which further complicates assessments. Others agreed, emphasizing the importance of considering financial health rather than solely vacancy rates. Several attendees highlighted the nuances of shadow and sublease space, where tenants might vacate early but continue paying rent to offset costs through subleasing. This scenario often indicates future poor performance when leases expire.

There was also a discussion about multifamily versus office spaces. An attendee

emphasized that vacancy metrics for multifamily buildings differ due to factors like expiring leases and rent adjustments to stimulate demand in tough economic conditions. This underscored the idea that vacancy rates serve as proxies for economic health. Another attendee suggested consulting brokerage experts for more accurate context about vacancy data, which could range from 17% to 35% in some markets.

OSE acknowledged that vacancy rates are a blunt tool and emphasized the importance of providing straightforward paths for extensions while offering other tools for flexibility. One person proposed asking downtown property owners to define a balanced market vacancy rate, which could serve as an indicator. OSE responded by asking if setting the metric too low might create disincentives, such as landlords maintaining vacant spaces to avoid compliance. Attendees noted that financial pressures like loan covenants could discourage such behavior, though it might still occur at the margins.

Several participants highlighted the complexities of choosing a specific vacancy rate, noting variations in financial impact based on ownership type and suggesting a broader range of metrics might be more appropriate. OSE explained that BEPS is only one part of the financial puzzle for buildings and emphasized the importance of keeping the extension criteria grounded in immediate hardship, avoiding unnecessary complexity.

The conversation also touched on alternative approaches. An attendee suggested using a metric like ENERGY STAR's time-weighted occupancy, which calculates occupancy over a defined period. OSE clarified that the ordinance defines the extension period as a consecutive 12 months within the 36 months preceding the compliance period. Another attendee pointed out that smaller spaces are leasing better than larger ones, and tenants are increasingly factoring the cost of potential capital upgrades into their leasing decisions.

Participants discussed the potential of using rent rolls as a simple and effective metric for assessing financial hardship. Others suggested incorporating total floor space and tracking trends over time. An attendee referenced the Living Building Pilot Program's occupancy rate requirement as a potential model for BEPS extensions. OSE noted that there is already a financial hardship pathway for buildings, reinforcing the idea that any additional metrics should remain simple and easy to administer.

#### **4. Deduction for district energy (steam)**

**Topic:** The ordinance states that (SMC 22.925.120) "Building owners may deduct the sum of the annual GHG emissions from the following end uses from their compliance GHGI, for one or more compliance intervals."

One available deduction is for district energy steam, hot water and/or chilled water provided by a private district energy provider. This is available for any covered building with a contract in place before June 1, 2024 for district thermal energy with a private district energy provider may deduct emissions from steam, hot water and/or chilled water from compliance GHGI. It is available only in the 2027-2030 and 2031-2035

compliance periods. All buildings must demonstrate the current district energy use and evidence that the contract was established prior to June 1, 2024.

To take the deduction, all buildings must submit:

- Energy meter data for the required BEPS reporting interval from a private district energy meter is tracked in ENERGY STAR Portfolio Manager.
- Evidence in ENERGY STAR Portfolio Manager of current automated upload from the private district energy provider via a “Data Exchange” property share OR a copy of a bill for the required BEPS reporting interval if the data is being manually entered.

In addition, one of the following must be provided to confirm the contract was established prior to June 1, 2024:

- A copy of a bill dated prior to June 1, 2024, showing service was provided at the building’s address.
- An affidavit from the private district energy provider stating service was provided at the building’s address prior to June 1, 2024.

### **Discussion:**

One attendee asked whether there would be a portal for retrieving historical energy usage data. A representative explained that billing services have transitioned to EnergyCap software, which will provide access to building data starting in 2024. Historical data prior to 2024 will not be included in the system, but invoices are available on file if needed.

OSE clarified that detailed energy usage data will only be required closer to compliance cycle deadlines. Data from before 2024 is only necessary as proof of service, not for detailed energy usage information.

## **5. Compliance with private building portfolios**

**Topic:** The ordinance (SMC 22.925.100) states that “Building owners with a building portfolio, district campus, or connected buildings may use an aggregate standard GHGIT for the covered buildings within the building portfolio, district campus, or connected buildings using the calculations in Section 22.925.080.”

Per BEPS (SMC 22.925.020) "Building portfolio" means two or more covered buildings on one or more lots, all owned by the same public, private, or nonprofit entity. Building portfolios may include district campuses and/or connected buildings. For the purposes of this definition, a building management company does not constitute an owner.

The buildings comprising a Building Portfolio generally function independently of each other and have separate meters and no district systems. They are distinct and usually dispersed geographically, but under the same ownership.

Building portfolios can comply using an aggregate standard GHGIT. “Aggregate standard GHGIT” means that these buildings can set and meet their GHGIT, based on a pro-rated mix of spaces for all their buildings’ square footage combined, in lieu of building by building compliance.

Per BEPS (SMC 22.925.020) “building owner” means an individual or entity possessing a fee interest in a covered building. However, private sector buildings are often registered as LLCs as part of the public record. For example, 123 Orca St. LLC and 456 Salmon Way LLC may both be owned by Puget Sound Properties. OSE has heard of three options for proving ownership of multiple buildings:

1. All buildings in the proposed portfolio have the same Owner as listed in the records of the King County Department of Assessments.
2. Owners provide copy of deed showing LLC is part of parent company or the title transfer of the LLC to the parent company.
3. Corporate secretary for owner provides a signed certificate affirming that they are the majority owner of a property.

OSE asked the attendees to share their level of support for the proposed methods of proving ownership.

### **Discussion:**

During a discussion about ownership and compliance under the ordinance, one participant noted that the term “owner” could be unclear, as individuals may have different percentages of ownership across a portfolio. They suggested that using “majority owner” might address this issue. Another attendee raised concerns that the ordinance might create obstacles for multi-owner district energy solutions, citing Amazon’s district energy project with the Westin Exchange data center as an example. OSE acknowledged that such cases are rare, emphasizing that it’s essential for someone to be responsible for managing a portfolio and ensuring that LLCs within the portfolio are aware of how compliance affects them.

Questions arose about the flexibility of compliance paths, with one attendee asking whether owners could switch from a portfolio approach to individual compliance later. OSE confirmed that portfolio ownership often changes and that switching to individual compliance would remain an option. Another participant expressed curiosity about how the ordinance accounts for the stability of ownership over time, noting potential challenges in notifying LLCs for each compliance cycle. OSE responded that frequent communication among owners and the need to share energy data would likely mitigate such issues.

Additional concerns were raised about the implications of selling buildings within a portfolio. One participant asked whether a grace period would apply to new owners. OSE noted that the existing tune-ups program includes a one-year grace period and explained that when a building is sold, the portfolio would need to be recalculated.

However, they acknowledged the need to determine how the new owner would be impacted. Another attendee cautioned that if the ordinance created significant burdens for selling assets, it could discourage owners from pursuing the portfolio compliance path.

Throughout the discussion, participants expressed varying levels of familiarity and commitment to the concepts, with some attendees seeking additional clarity before making decisions.

## 6. Custom decarbonization plans

**Topic:** A custom decarbonization plan enables nine additional years from 2041 to meet net-zero or low emissions for largest commercial buildings.

This option is available to building owners if:

- They face extenuating circumstances
- Meeting the compliance schedule/GHGITs would be a significant hardship

To comply via a decarbonization plan, building owners must demonstrate eligibility, apply to use the plan, and complete an energy & emissions audit.

### Discussion:

1. Catherine Stanford: Thanks everyone. OSE has always been open to feedback. Is there a definition for net zero? Also, BOMA measuring standards might be best for measuring buildings.
2. OSE: OSE is getting the BOMA standard measuring documentation as we are considering the standards for benchmarking measuring guidance.
3. Rod: I'll get you a copy.
4. OSE: There are a variety of definitions for net zero out there, but if it's free of fossil fuels it's generally net zero. However, BEPS includes end-use deductions such as for generators that move us beyond more standard definitions. Net zero GHGI targets can be defined for future rule.
5. Rod Kauffman: The White House has reached out to BOMA to define net zero. We can get you the paper on that topic.
6. OSE: EPA has a definition including free of fossil fuels and high efficiency. There's a specific definition in the ordinance but I don't have it handy.
7. Rod Kauffman: Will we do this again? I appreciated having the chance to speak and with such good representation of the CRE sector.
8. OSE: I think we will, but it's not confirmed.
9. Tony Toppenberg: There's a lot of different things impacting commercial real estate right now, and it adds additional complexity to legislation. Our portfolio might not quite meet the definition for substantial alterations but we will have significant capital expenses.
10. OSE: To reduce administrative burden reviewing a lot of plans, the City needed some guard rails in the law about eligibility criteria. There are a lot of criteria in

the ordinance, so we'll share those out and we can talk more about these options.

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