

## GENERAL OVERVIEW ESG

### 1 GENERAL INTRODUCTION

ESG (Environmental, Social, and Governance) considerations have gained prominence as fundamental criteria for assessing the sustainability and ethical impact of business operations and investments. Regulatory frameworks concerning ESG are introduced by the European Union (EU) – by way of several directives and regulations – with the aim to reach the goals agreed upon as part of the European Union's Green Deal (targeting no net emissions of greenhouse gases by 2050) and the Fit for 55 package (targeting a reduction of net greenhouse gas emissions with at least 55% by 2030). The built environment accounts for a large part of carbon emissions and, naturally, the regulatory frameworks also affect the real estate world. As such, investors, owners, users, asset and property managers and other parties in the real estate space are confronted with a lot of new topics and rules to abide by and act upon.

As ESG is a broad term, it is challenging to provide a comprehensive overview of any and all relevant ESG rules and regulations affecting real estate. This general overview focuses on providing an outline of the most conspicuous existing and future rules and regulations within the field of ESG and real estate, both at an EU and at a national level.

### 2 SFDR

#### 2.1 Introduction

The Sustainable Finance Disclosure Regulation (**SFDR**) is a regulation issued by the EU, which entered into force on 10 March 2021 and regards sustainability reporting. Since the SFDR is a regulation, it is directly binding and applicable across the Member States. It requires, among other things, financial market participants and financial advisors to be transparent about their approach on incorporating sustainability risks. It also requires these parties to evaluate adverse sustainability impacts of their investment decision or investment advice. These disclosures must be made on their website, in pre-contractual disclosures, and in annual reports.

The purpose of the SFDR is to (i) allow investors to make better informed decisions when determining which products fit their sustainability needs when selecting investment products, (ii) counteract "greenwashing" (making an investment product appear more sustainable than it actually is), and (iii) harmonise disclosure requirements within the EU. To reach these goals, the SFDR imposes disclosure obligations both at financial product level and entity level.

## 2.2 Product level disclosures - classification of financial products

The SFDR classifies financial products into three categories:

- (a) financial product without a sustainability ambition (Article 6);
- (b) financial product that promotes environmental or social characteristics, so-called light green products (Article 8);  
or
- (c) financial product that has sustainability and/or social investment as its objective, so-called dark green products (Article 9).

The more ambitious the product, the stricter the disclosure requirements are under the SFDR. The SFDR regulatory technical standards (**RTS**), effective from 1 January 2023, further outline the disclosure specifics. The annexes in the SFDR RTS provide templates for disclosing information related to Article 8 or Article 9 products.

## 2.3 Entity level disclosure - PAI statement

The SFDR can obligate financial market participants and financial advisors to issue a Principle Adverse Impact statement (**PAI statement**), a sustainability declaration. This is a "comply" or "explain" clause, giving them two options: to consider PAIs and explain how ("comply"), or not and clarify why ("explain"). Companies with over 500 employees do not

have a choice in this regard and must consider PAIs. This PAI statement must be published on the financial company's website by June 30 of each year. The SFDR RTS prescribes a template for this PAI statement, requiring info on at least 20 PAIs. Notably, two mandatory PAIs relate to real estate: (i) exposure to fossil fuels through real estate assets and (ii) exposure to energy-inefficient real estate assets. The template also provides for a number of voluntary PAIs related to real estate to consider, such as energy consumption intensity and waste production in operations.

## 3 EU TAXONOMY

### 3.1 Introduction

The EU Taxonomy Regulation (**EU Taxonomy**) entered into force on 1 July 2020 and is a regulation that describes a framework to classify economic activities performed in the EU as 'green' or 'environmentally sustainable'. Since the EU Taxonomy is a regulation, it is directly binding and applicable across the Member States. The classification system purports to assist investors to understand how sustainable a financial product is.

In case a financial product is offered, whereby the underlying investments of which are in economic activities that qualify as environmentally sustainable according to the EU Taxonomy, information should be disclosed to substantiate that qualification. The information should specify the environmental objective or objectives to which the economic activities

contribute. It should also stipulate the extent of environmentally sustainable activities; in other words, how “Taxonomy-aligned” the product is. In that context, the proportion of underlying environmentally sustainable activities related to the product should be presented as a percentage of the total underlying activities. When the criteria for environmentally sustainable activities are not considered, the party offering the financial product should provide a statement to that effect.

### 3.2 Environmental objectives

The focus of the EU Taxonomy lays on the following six environmental objectives:

- (a) *Climate change mitigation*: focusing on the stabilisation of greenhouse gas emissions and consistency with the long-term temperature goal of the Paris Agreement.
- (b) *Climate change adaptation*: focusing on the reduction or prevention of adverse impact of the current or expected future climate.
- (c) *The sustainable use and protection of water and marine resources*: focusing on sustainable use and protection of water and preventing or solving water scarcity and droughts.
- (d) *The transition to a circular economy*: which can be achieved in various ways, for instance by increasing durability and reusability of products or reduce the use of resources through the design and choice of materials of

a product but also through creating ‘product as a service’ business models.

- (e) *Pollution prevention and control*: focusing on avoiding the use of certain materials or products that (may) cause pollution, improving levels of air, water or soil quality and cleaning up litter and other pollution.
- (f) *The protection and restoration of biodiversity and ecosystems*: which can be achieved in various ways, for instance by provision of food and water, control of climate and disease, production of nutrient cycles and oxygen and provision of spiritual and recreational benefits.

### 3.3 Criteria to qualify as environmentally sustainable

To be classified as an environmentally sustainable or green activity according to the EU Taxonomy, an eligible economic activity should meet four overarching criteria. It should:

- (i) substantially contribute to one of the environmental objectives outlined above;
- (ii) do no significant harm to the other five environmental objectives;
- (iii) meet the so-called ‘minimum safeguards’ such as the UN Guiding Principles on Business and Human Rights to not have a negative social impact; and

- (iv) comply with the technical screening criteria.

The scientifically based technical screening criteria (item (iv)) are in fact an elaboration of items (i) and (ii). They are being established by the European Commission to provide for the legal clarity to assess if an activity is compliant. In other words, the technical screening criteria describe – in technical detail – when an activity provides a substantial contribution to a certain environmental objective (item (i)), and when an activity does no significant harm to a certain environmental objective (item (ii)).

The technical screening criteria are being elaborated in secondary legislation called Delegated Acts. In December 2021, the Climate Delegated Act was released describing the criteria for a substantial contribution to the objectives ‘climate change mitigation’ and ‘climate change adaptation’ for approximately 102 economic activities. The do no significant harm technical screening criteria for these economic activities have been worked out and released for all objectives in the Climate Delegated Act.

The 102 economic activities for which technical screening criteria have been detailed in the Climate Delegated Act are activities within various sectors. These include transport, construction & real estate, manufacturing, and energy. There are three main economic activities relevant to the real estate sector that fall within the scope of the EU Taxonomy. These are (i) acquisition and ownership of buildings, (ii) construction of new buildings and (iii) renovation of existing buildings. This means that a large portion of real estate transactions is in

scope of the EU Taxonomy.

In June 2023, the Environmental Delegated Act was adopted by the European Commission describing the criteria for a substantial contribution to the objectives (i) the sustainable use and protection of water and marine resources, (ii) the transition to a circular economy, (iii) pollution prevention and control and (iv) the protection and restoration of biodiversity and ecosystems, but in each case only for a selection of economic activities. Economic activities and sectors that have been identified as having the biggest potential to make a substantial contribution to one or more of the four environmental objectives are covered. The economic activities construction of new buildings and renovation of existing buildings are covered by the Environmental Delegated Act. The Environmental Delegated Act has been submitted to the European Parliament and the Council of the EU for scrutiny and will not enter into force until it has been published in an Official Journal.

## **4 CSRD**

### **4.1 Introduction**

In 2014, the NFRD introduced an obligation for large public interest entities in Member States to include a non-financial statement in their management reports. The non-financial statement was to provide transparency on policies related to, among other things, environmental, social, and personnel matters, as well as companies’ efforts to respect human rights to combat corruption and bribery, and the impact of these

issues on their business operations. The Corporate Social Responsibility Directive (CSRD), which came into effect on 5 January 2023, revises sections of the Accounting Directive relating to non-financial disclosures that were introduced by the NFRD. The CSRD must be implemented into national law by 6 July 2024 and thus become part of the Member States' laws. The Dutch legislator has published draft legislative instruments to transpose the CSRD into Dutch law. It is still uncertain whether the Netherlands will meet the implementation deadline. The objective of the CSRD is to ensure adequately publicly available information about the risks that sustainability issues present for companies, and the impacts of companies themselves on people and the environment. This should, among other things, enable investors to assess the sustainability of their investments, similar to one of the SFDR goals. Furthermore, the CSRD aims to improve the quality and comparability of sustainability information, to increase transparency and accountability and, to align sustainability reporting with the EU's sustainable finance agenda.

#### 4.2 Changes to reporting requirements

The CSRD brings about various changes, such as a significant extension of the scope of the (sustainability) reporting requirements and the introduction of a limited assurance statement on the sustainability report from a statutory auditor (or other independent provider of assurance services).

Central to the CSRD is the requirement to include a

sustainability report within the management report. This sustainability report must be included in a distinct section of the management report and clearly identified as such. The information provided in that section must cover the sustainability impacts from two perspectives, known as the double materiality perspective. The CSRD mandates companies to report both on the effects of their operations on the environment and society, as well as on how sustainability issues impact their business. As such, the risks and impacts of the company are each to be considered from a materiality perspective. In addition, the reporting is not limited solely to the sustainability of the company itself, but depending on the sustainability matter also includes the sustainability in the value chain which the company is part of. The sustainability report must be drawn up in accordance with the European Sustainability Reporting Standards (**ESRS**). The ESRS provide a uniform set of reporting standards and distinguishes between: (i) cross-cutting standards, (ii) topical standards and (iii) sector-specific standards. All companies falling within the scope of the CSRD will be required to report on the cross-cutting standards, which cover the reporting areas governance, strategy, impact, risk and opportunity management, and metrics and targets. The topical standards cover a broad collection of sustainability matters. This includes, among other things, providing information on policies related to ensuring equal opportunities for employees, climate protection, working conditions, human rights, business ethics and corporate culture. In principle, a company only has to report on the disclosure requirements under a topical ESRS when it has determined that the relevant

sustainability matter is material using the 'double materiality' assessment mentioned above. In July 2023, the European Commission adopted a delegated regulation containing the first set of ESRS comprising two cross-cutting standards and ten topical standards. The preparation of the sector-specific standards is likely to be postponed to June 2026.

The reporting requirements introduced by the CSRD will be phased in from 2024 to 2028. The exact scope of the requirements as well as timeline to comply with depend on within which category the company falls ('large', 'medium', 'small' or 'micro').

## 5 LEGISLATION ON ENERGY PERFORMANCE OF BUILDINGS

### 5.1 Energy label

Since 1 January 2008, the Energy Performance (**Buildings**) Decree (*Besluit energieprestatie gebouwen*) stipulates that each owner or landlord (apart from a short list of exceptions, which include offices with a total gfa of less than 50 m<sup>2</sup>, as well

as buildings which have been listed as monuments) is under the obligation to submit an 'energy performance certificate' for their building(s) to the purchaser or tenant in case of sale or letting out of the building. This certificate intends to provide the purchaser or tenant insight in the amount of energy required for the normal use of the building concerned. This Dutch legislation

on energy performance of buildings is derived from European Union legislation.

As of 1 January 2015, the obligation to submit an energy performance certificate has been replaced by the obligation to submit an 'energy label'. Not submitting a definitive energy performance label when selling or leasing out a building is subject to a fine up to € 450 in case of individuals and up to € 20,250 in case of legal entities. The competent body is the ILT (*Inspectie voor Leefomgeving en Transport*).

Since 2023, every office building in the Netherlands with a surface area of 100 m<sup>2</sup> or more must satisfy the (sustainability) requirements for at least energy performance label category C. Any office building that does not meet the requirements for a category C label, will be deemed unfit for use. Not having a category C label by 2023 could lead to a warning by the Municipal Executive, a penalty or even closing of the building.

The Energy Performance (**Buildings**) Decree is merged into the Environment Buildings Decree (*Besluit bouwwerken leefomgeving*) as of 1 January 2024, as part of the introduction of the Environment and Planning Act (*Omgevingswet*) as of that date. Under the Environment Buildings Decree, the aforementioned obligations will continue to apply, albeit on a different legal basis.

## 6 BENG

Furthermore, as of 1 January 2021, all applications for building permits (for residential and non-residential buildings) in relation to energy performance must comply with the requirements for Almost Energy-Neutral Buildings (*Bijna Energieneutrale Gebouwen - BENG*). BENG is based on Trias Energetica, which assumes the following energy performance indicators:

- (a) maximum energy requirements indicator expressed in kWh per square meter of usable surface area per year (BENG 1)
- (b) maximum primary fossil energy requirements indicator expressed in kWh per square meter of usable surface area per year (BENG 2); and
- (c) minimum proportion of renewable energy expressed as a percentage (BENG 3).

### 6.1 Energy saving measures

The Activities (**Environmental Management**) Decree (*Activiteitenbesluit milieubeheer*) obliges the operator of an establishment (*inrichting*) to implement all energy saving measures with a payback period (*terugverdientijd*) of less than five years. The obligation to implement such measures may be imposed on either the owner or the tenant of the property, depending on the factual situation. A list of so-called 'recognized measures' has been adopted for 19 different industry sectors. Some of the recognized measures are

building-related measures (e.g. the isolation of the facades), while other measures pertain to the use of the property (e.g. an energy-efficient use of printers and copying machines). The owner of the property would generally be expected to hold the responsibility for the implementation of building-related measures, whereas tenants are responsible for any energy-saving measures related to their operational activities. Furthermore, reports on the implementation of energy-saving measures need to be submitted to the relevant competent authorities (usually the municipal executive) ultimately by 1 December 2023, and once every four years after that date.

The obligation to implement all energy saving measures will continue to apply under the Environment and Planning Act as of 1 January 2024, albeit that the obligation is split across two separate decrees. For buildings with a use function, an obligation to implement all energy saving measures with a return on investment of five years or less has been included in the Environment Buildings Decree (*Besluit bouwwerken leefomgeving*). For so-called environmentally harmful activities (*milieubelastende activiteiten*), a concept which will replace the prior concept of a single 'establishment', the Environmental Activities Decree (*Besluit activiteiten leefomgeving*) lists whether (additional) energy saving obligations apply in respect of that particular activity.



## 7 EPBD IV

An important legislative instrument of the European Union in order to achieve its Paris Proof ambitions, is the Energy Performance of Buildings Directive (**EPBD**). EPBD III is currently in force and its latest updates have been incorporated into national regulations, mainly in building codes such as – in the Netherlands – the Dutch Building Decree (*Bouwbesluit*) and the corresponding energy label methodologies of Member States. EPBD III for instance introduced the concept of BENG as described above.

EPBD IV proposes to update the EPBD with the purport of achieving no net emissions of greenhouse gases by 2050. Expectedly, EPBD IV shall have to be implemented by all Member States by 2025.

Although the final wording of the EPBD IV is still to be published, some of the main proposed changes are:

- (a) Zero-emission buildings (*Energie neutrale gebouwen – ENG*) will become the standard for new buildings as of 2028, as opposed to the BENG norm which is currently implemented.
- (b) The energy label ratings are harmonized at an EU level. A-ratings will be reserved for ENG buildings and G-ratings are for the 15% worst performing buildings in a given market, with the remaining buildings in the country distributed proportionately among the classes in

between. Ratings are to be based on actual energy usage rather than theoretical measurements.

- (c) Minimum energy performance standards are introduced for nonresidential buildings and potentially also for residential buildings.
- (d) If technically and financially feasible, solar panel systems should be applied on all nonresidential buildings as from 31 December 2026.
- (e) The validity of energy labels will change; labels with class C and above will be valid for 10 years and class D and below for only 5 years.
- (f) The introduction of a 'building renovation passport'. These passports should entail specific renovations that need to be implemented for a building to reach net zero by 2050 at the latest and indicate expected benefits in terms of energy savings and greenhouse emission reductions. The passport shall be issued by a qualified and certified expert based on input from (an) on-site visit(s).
- (g) National governments are required to establish long-term renovation strategies to decarbonize the national building stock by 2050. National goals should be linked to EU goals (with milestones against 2030, 2040 and 2050) considering the emissions of the buildings over their entire life cycle. The national renovation plans should



include ways of financing and funding needed to make the improvements to the building stock. The national governments should furthermore provide for an overview of building stock in their country, an energy label data base, building renovation passport content and calculated /metered energy consumption.

It should be noted that the EPBD IV and the EU Taxonomy could be regarded connected. In the EPBD IV, explicit

reference is made to the EU Taxonomy for criteria related to building renovation activities. This means that alignment with the EU Taxonomy is relevant for compliance under the EPBD IV.

The framework as set out above has been (and will be) implemented in the Environment and Planning Act and related decrees going forward as of 1 January 2024, primarily the Environment Buildings Decree (*Besluit bouwwerken leefomgeving*).

## 8 ENVIRONMENTAL LABELS AND ASSESSMENT METHODS DUTCH REAL ESTATE

There are several methods in use in the Netherlands for assessing the environmental impact of real estate. The parties to (turnkey) sale and purchase agreements, building contracts or (green) leases often refer to such 'labels' in their contracts setting sustainability requirements or rankings the real estate

must meet. Frequently, reference is made to the Building Research Establishment Environmental Assessment Method (**BREEAM**). In the Netherlands, BREEAM labels are granted by the Dutch Green Building Council. Nine sustainability categories of management form part of the criteria assessed in the context of BREEAM: Management, Health and wellbeing, Energy, Transport, Water, Materials, Waste, Land use and

ecology and Pollution. Other sustainability rating systems are the Leadership in Energy and Environmental Design (**LEED**), Global Real Estate Sustainability Benchmark (**GRESB**) and WELL. It should be noted that these labels with specific rankings for real estate are not mandatory but often a certain standard is self-imposed by the contracting parties involved.

Another assessment method used to measure if the energy consumption and carbon dioxide emission of a building remains within the Paris Agreement – aiming to keep the global temperature rise this century to 2 degrees Celsius above pre-industrial levels and to pursue efforts to limit the temperature increase even further to 1.5 degrees Celsius – is the Carbon Risk Real Estate Monitor (**CRREM**). CRREM is an international initiative for commercial real estate and has been set up based on the carbon dioxide budget. Within CRREM, the CRREM pathways have been defined. Assessments can be made to establish if the energy consumption and carbon dioxide emission of a real estate asset remains under the line of the pathways. If the asset does not remain under the line, it is regarded as a 'stranded asset'.

## **9 ENERGY CONGESTION**

In many regions of the Netherlands, the electricity grid is becoming increasingly busy, often leading to congestion issues for developers, owners and users of real estate. This congestion primarily arises due to an increasing demand for transport capacity on the grid, surpassing the capacity available on that part of the grid. This situation becomes particularly problematic when developers, owners and users of real estate seek to increase the connection and/or transmission capacity on the grid at a building to, for example, cater for specific usage requirements or implement sustainability measures (such as changing from gas heating to electric heating or the installation of a solar panel system). Consequently, real estate owners and users may encounter obstacles when attempting to increase connection and/or transmission capacity, potentially hampering their ability to implement sustainability measures.

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