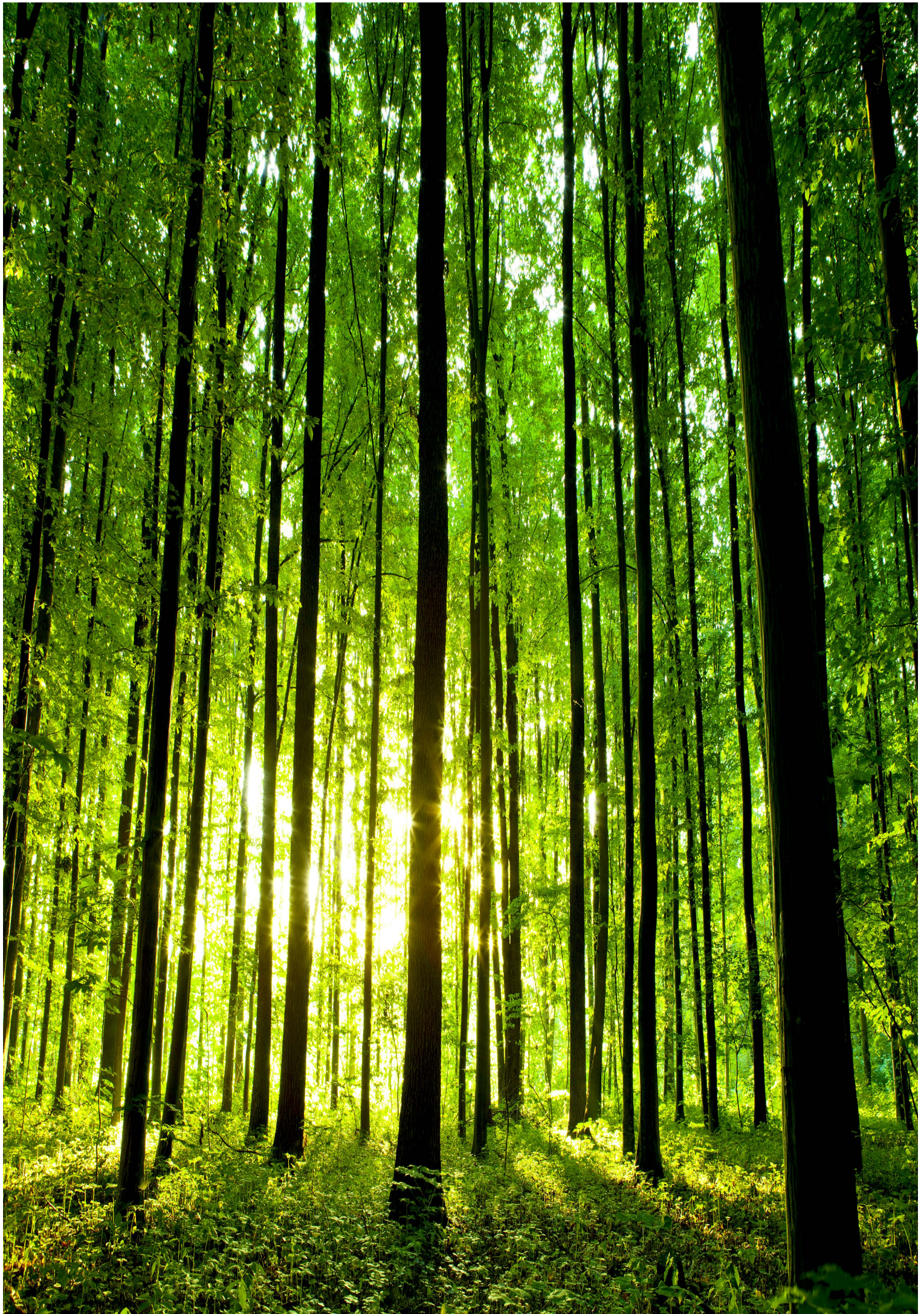




Creating sustainable value
ESG Real Estate Insights Vol. 2



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Executive Summary

In the light of climate change and other pressing ecological problems, sustainability has become one of the most important global issues. It has massive significance for the real estate industry as well. Considering the considerable carbon footprint of the real estate value chain, sustainability is now a top risk priority for the sector – not least because of new and upcoming ESG regulations.

ESG is here to stay. The Real Estate industry has to take action – now!

In recent years, an increasing number of climate-related incidents has captivated the attention of global audiences. Social issues across supply chains are hotly debated, corporate governance is scrutinised ever more closely. Sustainability is surely here to stay – and as market participants, governments and the wider public demand effective corporate action, the real estate industry needs to proactively address ESG themes in all its dimensions. Given the urgency of action towards reaching global climate goals, the environmental dimension is particularly important. In 2020, buildings accounted for 37 percent of global energy-related carbon emissions.¹ Accordingly, investors, owners, assets managers and other real estate players are confronted with a raft of transformational topics and new regulations. In this report, we present seven expert contributions to shed light on the most important current developments.

After the introduction of the EU Sustainability Financial Disclosure Regulation (SFDR) and the EU Taxonomy, the industry now needs to tackle regulatory issues around the classification of funds in terms of ESG characteristics and objectives, and around new disclosure requirements (Article 1, p. 07). As to the Taxonomy, reporting alignment becomes a major priority for the near

future, depending on individual eligibility. Developers need to consider externalities such as circularity quotas, and to update business IT tools in order to document alignment; asset managers are tasked with climate risk assessments (Article 2). The updated RICS Valuation Guidance Note on Sustainability and ESG asks property valuers to explicitly address ESG factors in the justification of their judgements in qualitative terms. Valuers should consider relevant benchmarks and could benefit from tools such as the Carbon Risk Real Estate Monitor (CRREM) (Article 3).

From 2024, the Corporate Sustainability Reporting Directive (CSRD) will require companies to report on non-financial (ESG) themes based on their materiality. Organizations should analyse their themes and set targets, define respective KPIs and create an overview of the necessary ESG data. Gathering this data is not trivial, as sources across the ecosystem have to be identified and collection methods devised (Article 4). Real estate companies aiming at a more effective and stringent approach to decarbonization should consider the Science-Based Targets initiative (SBTi). It offers a valuable framework and is already applied by nearly 3000 companies globally (real estate: 156 companies). The scheme requires companies to calculate baselines and set operational boundaries. On the path to net zero, carbon

accounting represents a critical first step, addressing both operational and embodied carbon (Article 6). In order to facilitate the industry's sustainability transformation, Deloitte has developed a proprietary Digital ESG Assessment based on regulatory requirements. The assessment covers the entire real estate life cycle, addresses all three ESG dimensions and includes state-of-the-art tool support for gathering data, gaining transparency and identifying options for action (Article 7).

We wish you many interesting insights while reading and will be happy to answer any question you may have.

Kind regards,

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¹2021 Global Status Report for Buildings and Construction, developed by Global Alliance for Buildings and Construction for the UN Environment Programme.



Real estate's need for regulatory compliance with ESG goals

In the last years, regulations with regards to ESG such as the SFDR and Taxonomy regulation have shaped the real estate industry, says our ESG specialist from Luxembourg Dario Zambotti.

Looking forward, we see that this development will continue: One year after the effective date of SFDR, the classification of real estate funds based on their ESG characteristics and ESG objectives (article 8, article 9 funds) is a challenge the industry is facing today. Other challenges are SFDR and Taxonomy disclosure requirements as well as data management and use.

However, every item to tackle today is also another important step in the ESG transformation journey.

Alignment with the future: Real estate's need for regulatory compliance with ESG goals.

The real estate market is addressing environmental, social, and governance matters from many different angles: adopting different strategies, seeking different positioning, serving investors' different needs.

The application of both the Sustainability Financial Disclosure Regulation (or "SFDR" in short) and the Taxonomy Regulation have certainly generated a drive towards improving the long-term focus on the pillars of ESG.

The hot topic today, now 1 year after the effective date of the SFDR, is the classification of real estate funds based on their

ESG characteristics and ESG objectives: Recently ESMA and INREV clarified that art 9 products should hold only sustainable investments. This means that the funds having the objective to improve the environmental impact of non-sustainable buildings should be classified as art 8 products.

In addition, there are still many questions with no clear answers: How to determine a sustainable investment? Which considerations apply to the "do not significantly harm" principle? How to calculate the taxonomy alignment? Which level of performance, which level of emission, which type of certificates would allow to meet the requirements?

Another challenge to confront refers to SFDR and Taxonomy disclosure requirements which are applicable since January 2022 – which covers disclosure in annual report and additional non-financial reporting to stakeholders on certain KPI's.

This leads us to the main issue – one that many organisations struggle with in the day and age: Data.

Data is integral and it is necessary to identify the material information needed to implement policies, procedures and controls to report meaningful information to investors. At Deloitte we are assisting

clients in finding a robust approach to identify data points, ensure reliability, efficient collection of data and ultimately produce effective reporting.

The real estate industry clearly has a very important role to play in the ESG transformation of our economy: It has the opportunity to leverage a clear alignment of the industry's long term goals with ESG matters to the all the stakeholders in the entire value chain. It is an opportunity to take today.

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Watch the
video here



EU taxonomy: towards alignment

Now that large real estate companies have released their non-financial statements including the reporting on EU taxonomy, the focus is shifting towards reporting alignment. The Real Estate industry is facing major challenges to prepare an aligned EU taxonomy reporting, including a risk analysis, a review of the IT tools and the impacts of this regulation on the strategies of asset managers and developers.

Most large real estate companies¹ are about to publish (if they have not already) their Universal Registration Document, which will include for the first time a specific part regarding their eligibility to the EU taxonomy on their non-financial statement. As a reminder, to have eligible activities means that the company generates Turnover or has CapEx or OpEx related to an activity described in one of the 2 annexes already published (mitigation² and adaptation³ to climate change).

Publishing the ratio of eligibility of Turnover, CapEx and OpEx already generated diverging interpretations across countries. If there may be tolerance and understanding from the European Securities and Market Authority (ESMA) for these first publications, it is reasonable to assume that they will be more demanding as the European Commission is clarifying the requirements and interpretations in the coming years as the focus shifts towards alignment.







Fig. 1 – The main steps of compliance to taxonomy



Perimeter of Eligible Activities

Scientific approach to the selection of activities

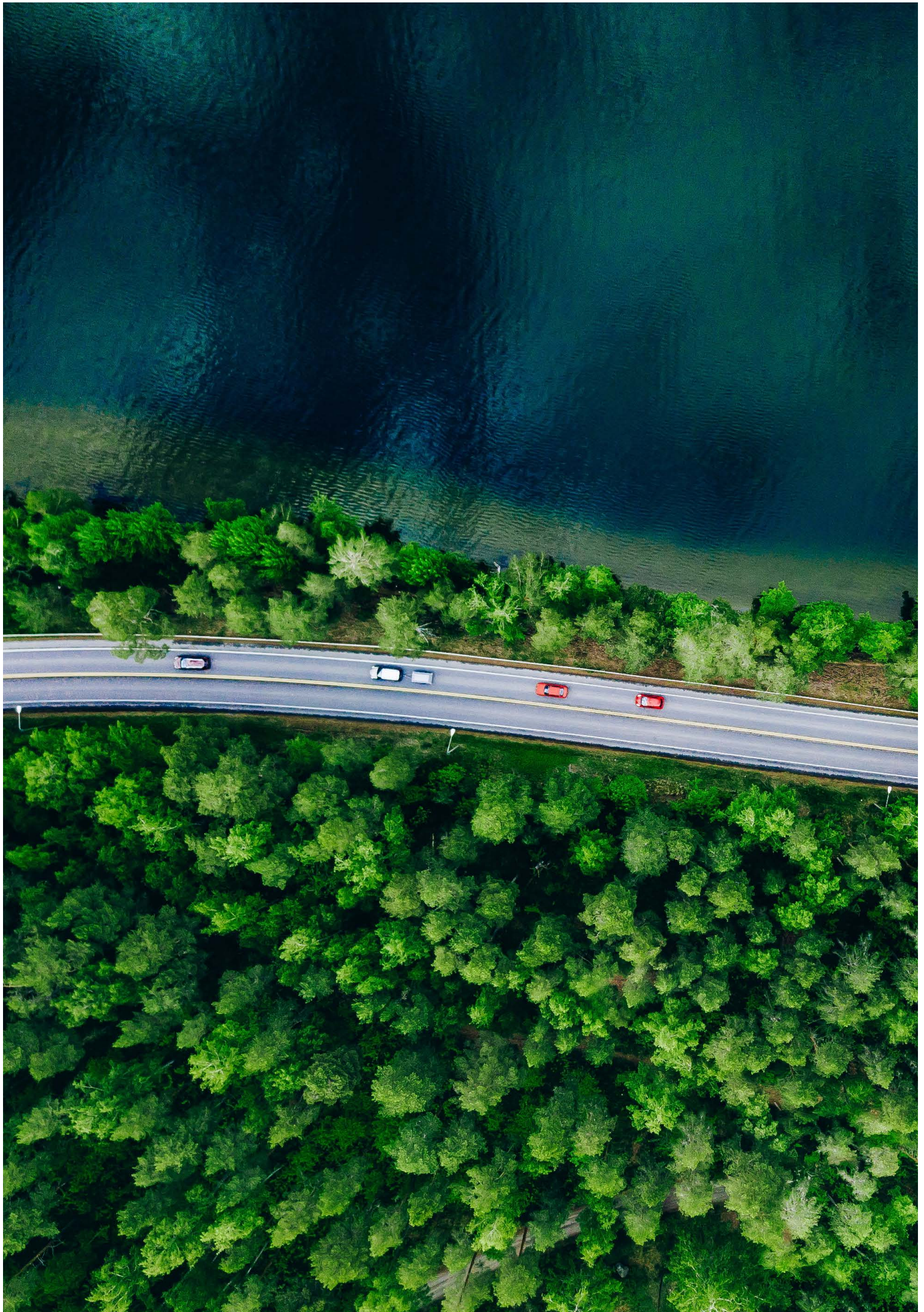
Environmental Objectives

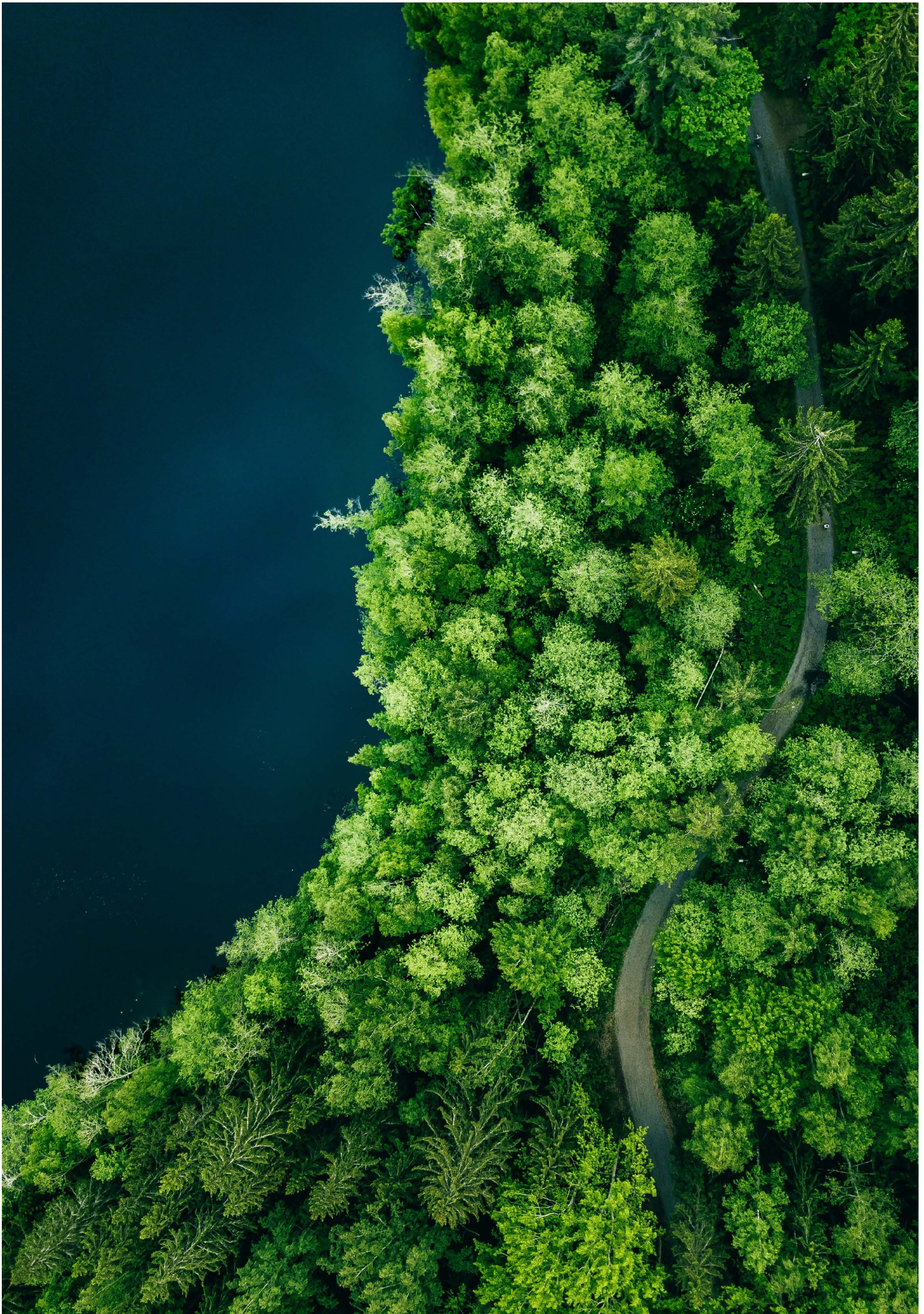
-  **1** Climate change mitigation
-  **2** Adaptation to climate change
-  **3** Sustainable use and protection of aquatic and marine resources
-  **4** Transition to a circular economy
-  **5** Pollution prevention and reduction
-  **6** Protection and restoration of the biodiversity and ecosystem

Green financial KPIs

- Share of green TO
- Share of green CapEx
- Share of green OpEx
- Exhaustive Contextual Information







The real estate industry is facing multiple challenges to be able to define their alignment for next years:

For developers:

- Their processes need to evolve to take into consideration new externalities that generate new costs (for example: measurement of biodiversity impacts, minimum rate of 70 percent of circularity in waste generated, mandatory Global Warming Potential (GWP) consideration, etc.).
- They have to update their business IT tools in order to trace and to account for each piece of evidence of the alignment corresponding to each and every Technical Screening Criteria. This would require an interface between these tools and the financial consolidation IT tools to ease reporting.

For Asset Managers and Developers:

- They will have to conduct a specific "robust climate risk and vulnerability assessment" of their assets in stock or construction sites.⁴

Most of these new obligations are not present in national regulations and the speed of each government to translate the EU directives (defining some of these obligations) into their respective national regulations already has an impact on alignment country by country. For example, a life cycle analysis is now mandatory in France for every new construction. It provides the Global Warming Potential seen earlier. This is not yet the case in other EU countries.

However, even if stakeholders adapt their processes to these new objectives really fast, the ongoing projects, based on a previous set of less demanding rules, will generate turnover impossible to align for at least two years. Therefore, it is already safe to say that most developers who reported a strong eligibility ratio will have a very close to zero alignment next year and a steady improvement going forward after that before reaching their adequate level. From a governance

perspective, according to the recent draft of the annex to the platform on Sustainable Finance report,⁵ Boards will need to accept and implement the changes required to aim perfect alignment in construction of new buildings (7.1) and renovation of existing buildings (7.2) in 2024, and if possible, even sooner.

The length of the construction cycle (invoicing over several years) has another implication for the characterization of the alignment. Indeed, promoters will receive calls for funds from theoretically aligned operations before being able to deliver proof of this alignment, since it can only be provided on delivery (e.g Energy Performance Certificate).

Nevertheless, we can make an educated guess that the characterization of the alignment will probably be divided into two phases:

- Phase one before the delivery, when the developer will commit to the alignment, and
- Phase two thereafter, when one will be able to prove it.

There are some interesting developments in the recent draft of the annex regarding other objectives, substantial contribution to circular economy is being clarified for both new constructions and renovations. If it is confirmed, it might offer an alternative for projects aiming (only) Nearly Zero Energy Building (NZEB) level and not NZEB – 10 percent even if the requirements in terms of circular economy are important (design, integration of reused and recycled materials, 90 percent of waste prepared for re-use and recycling). The final version of the text is being expected in the first semester of 2022 and it might have an impact on the chosen strategy by developers to align their programs.

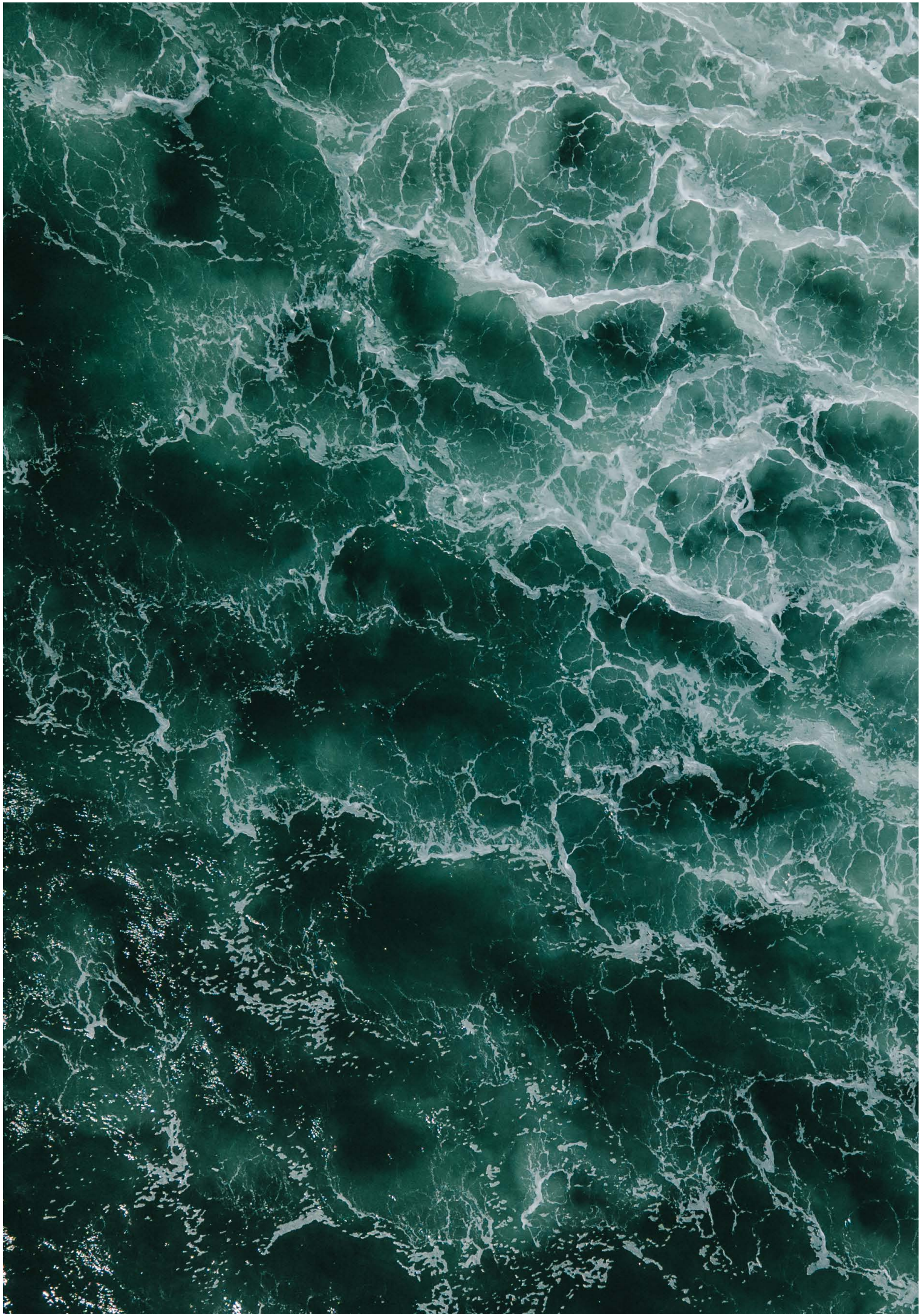
As the first taxonomy reportings are published by companies, the European Commission may continue to share the correct

interpretations through its FAQ section and adjustments will probably need to be made to the strategies of asset managers and developers. The sooner the identification of those adjustments are made, the faster the rectifications on strategies will be. The close monitoring of those changes remains an important consideration throughout the process.

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ESG: The valuer's moment has arrived

The rapid evolution of the ESG agenda and its increasingly direct impact on real estate industry is challenging the traditional role of the valuer. Notwithstanding the scarcity of explicit and authoritative market evidence, the agenda is influencing the choices and decisions of all participants and stakeholders within the real estate market.

A key driver of this is the trajectory of much of the regulation and legislation which not only seeks to enhance compliance and standards but through significantly enhanced reporting transparency – particularly with regard to risk exposure – to catalyze and inform ESG-aligned choice. The recently published update to the RICS Valuation Guidance Note on Sustainability and ESG echoes this approach by effectively requiring valuers to articulate how ESG factors have influenced the judgments they have made in forming their opinion(s) of value. While such articulation may currently be reliant on “qualitative” rather than “quantitative” perspectives, this evolution of practice is one which is consistent with a valuer's need to remain entirely objective and independent yet provides an exciting opportunity for valuers to professionally contribute to the ESG agenda.

It is an exciting time to be a real estate valuer. With the ESG agenda having gained center stage across virtually every facet of both business and daily life, it is beyond doubt that valuers can – and must – play an important role in enabling and effecting change.

To date, pointing the finger at valuers in the quest to see ESG aspects recognized “in the numbers” has been rightly responded to that the core role of the valuer is as a “score-keeper” rather than a “score-maker”. In other words, the phrase serves as a reminder that valuers have no mandate to bring personal prejudices to bear when expressing an opinion of Market Value – or Fair Value. The definitions of Market Value and Fair Value essentially require a valuer to dispassionately consider what the highest or best bids received from the market by an asset owner, who in turn is a willing seller, will be. Another way of viewing this “process” is that a valuer must effectively step into the shoes of the hypothetical purchaser – and it is through this lense that the activities required of a valuer in respect of ESG issues can be seen to be evolving at pace and also where it is clear that a valuer does indeed have a role to play in a world where ESG objectives have taken center stage.

In the case of real estate held for investment purposes, value is of course “created” through its ability to deliver a rental income stream. The quantum of value is effectively a judgement as to the risk profile attaching to that ability to deliver, maintain and grow the income stream. Recognition of the ability for ESG related factors, such as energy efficiency, physical risks including flood or over-heating and transport connectivity through to measures that influence occupant wellbeing to influence that risk profile is now embedded across swathes of the real estate investment market. Indeed, it is not only recognized, but disclosure of approach and exposure is increasingly a pre-requisite of their various stakeholders – whether that are an investor’s own investors, lenders, regulators or market analysts.

The latest RICS Valuation Guidance Note addressing Sustainability and ESG issues within commercial real estate became effective on 31 January 2022. At its heart, the Guidance Note seeks to aid valuers in identifying and addressing ESG and Sustainability factors as they form their judgements. But so too does it raise the requirements placed on valuers to explicitly recognize the influence such factors have had on informing their judgements through commentary within valuation reports. The evidence base to provide empirical support as to the impact of ESG and Sustainability related factors is recognized to be limited (at best). Indeed the Guidance Note does not require or expect valuers to apply explicit adjustments within their valuations – unless evidence to do so demonstrably exists within the market pertaining to the asset under consideration such as identifiable capital expenditure to address minimum energy efficiency regulatory requirements or flood defence risks. The Guidance Note does however require valuers to “qualitatively” articulate the perceived risk profile of the asset. In so doing, the expectation is that the recipients of valuations will be able to take a better informed view of an asset’s risk profile...and in due course create the evidence upon which valuers will consider when forming their judgements.

This approach to disclosure and “transparency of thought” is consistent with the tightening aims and expectations of regulatory disclosure initiatives such as that set out by the Taskforce for Climate Related Disclosures and the EU Taxonomy related Sustainable Finance Disclosure Regulations. Indeed, the importance of this approach is reinforced by the following quote from Rt Hon Rishi Sunak MP, the UK’s Chancellor of the Exchequer:

“Investors and businesses must have the information they need to understand the full range of environmental risks they face and create. That information should be a key component of every investment decision and the strategy of every business. Climate and environmental considerations

should be central to the decision making process ...”.

Unsurprisingly, the valuer’s toolkit needs to evolve to respond to this shift in market dynamic. Requesting and considering a range of benchmark information such as BREEAM, LEED or NABERS, alongside Energy Performance Certificates to review Minimum Energy Efficiency Standards associated risks are examples. So too, increasingly, will be an affinity with tools such as the Carbon Risk Real Estate Monitor (CRREM) which seeks to provide visibility on decarbonization risks associated with achieving commitments contained within the Paris Agreement. Importantly, valuers are not, and nor will they be, Sustainability or ESG experts; just as they are not Building Surveyors, Contaminated Land experts or Town Planning specialists. However, as with absorbing and interpreting the insight from Building Surveyors, Contaminated Land experts or Town Planning specialists to consider the likely reaction of market participants, their role does now extend to the consideration of how Sustainability and ESG related information may influence the valuation of assets within their area of expertise.

So, the stage is set in 2022 for valuers to genuinely embrace Sustainability and ESG issues to engage in the agenda and to refine approaches accordingly. Having weathered the uncertainty storms of the global financial crisis and the COVID pandemic, ESG & Sustainability is now the priority.

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Get your real estate data straight, the CSRD is coming

The current negative impact of the real estate industry on the environment and the positive impact it could potentially have is significant. It is time to take responsibility and act. Besides environmental impact, ESG also covers plenty of social and governance themes, which could and should be improved in real estate industry.

To ensure climate neutrality in 2050 and to accelerate transparency in sustainability reporting, the EU puts legislation in place. This article will focus on the Corporate Sustainability Reporting Directive (CSRD). The CSRD improves transparency in a company's sustainability performance and will come into effect as of 2024 for fiscal year 2023 and is the successor of the Non-Financial Reporting Directive (NFRD). The CSRD is applicable for EU listed organizations and EU organizations meeting at least two of the following three requirements: i. more than 250 employees, ii. a revenue of at least € 40 m and iii. a total balance of € 20 m. This will affect 50.000 real estate companies in the EU among which many real estate related organizations.

Where to start as a real estate organization? ESG data. Data is crucial to improve the sustainability of organizations and to meet ESG reporting requirements such as those coming forward from the CSRD. However, making an overview of the required ESG data can be a complex and time-consuming exercise requiring specialist knowledge. The following paragraph will shed light on ESG data extraction and data management.

Being well-prepared for the CSRD and improving the sustainability performance starts with understanding the bigger picture, objectives, and consequences of organizations for their reporting framework. In order to do so, there are three key perspectives of great importance.

Overview of requirements: What data does my organization need to report on ESG performance?

The CSRD requires that organizations report on non-financial themes (ESG themes) where they can make the most impact. To do so, companies perform a materiality assessment identifying the ESG themes and business risks from a double materiality perspective. Materiality is the concept that defines why and how specific issues are significant for a company. By introducing the concept of “double materiality”, organizations need to consider both the impact of climate-related risk and opportunities on the company’s value (“financial materiality” or “inward impact”) and the external impacts of the company’s activities on the environment (“environmental and social materiality” or “outward impact”).

After determining which themes are material for organizations, three steps are essential to create an overview of requirements:

- 1. Companies have to analyze the current standing of the material themes and set their ambitions and targets.**
- 2. Companies have to define the KPIs required to reach these targets.**
- 3. Companies have to generate an overview of the data they need to report on these KPIs.**

The data required to measure and report on the KPIs might be available within the organization. However, a significant part of this non-financial data is only accessible

outside the organization (e.g., in a construction organization, when they want to know the greenhouse gas emissions from their suppliers during the transport of materials). Therefore, determining where to get the necessary data is the next step.

Position in the real estate ecosystem: From which sources should my organization collect its data?

Ownership of non-financial data organizations require could be widespread within the real estate industry. Therefore, the position of the organization in the real estate ecosystem is crucial to determining the data sources necessary for CSRD reporting. To get insight into dependencies, organizations have to create an overview of which other players in the real estate ecosystem impact their processes and if they are willing to disclose the data needed (e.g., a Real Estate Investment Trust wants to report on the energy usage of its portfolio, therefore, they need the usage data of their tenants). After completing this assessment, the next step is to determine how to collect the data from other players in the real estate ecosystem.

Accessibility through strategic partnerships: Which players should organizations work with to access all necessary data?

After creating an overview of the data sources and which players companies rely on to gather the data, it is time to define the necessary process of data collection, transformation, analysis, reporting, and identify required changes to the current process. This requires starting the dialogue with partners and other players in the real estate ecosystem to start strategic partnerships to share ESG data. However, to be successful, companies have to create clear incentives for all involved players within to ensure that all players gain from sharing and to make the partnership reliable. The success is also depending on the mutual agreements on the correctness and accuracy of the data shared.

Conclusion

The CSRD drives organizations to accelerate improvements on the ESG themes and to increase transparency in sustainability reporting. Sound ESG reporting requires good ESG data management. Creating an overview of required data, the position in the real estate ecosystem and accessibility through strategic partnerships are crucial perspectives.

Deloitte has experience in setting up ESG strategies, performing materiality assessments, assisting in the creation of strategic partnerships with respect to data sharing and can support organizations in these processes.

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SBTi: decarbonizing real estate in line with climate science

Each year, an increasing number of companies consider the impact that their offices, warehouses, and other premises have on the environment – therefore, they evermore require their buildings to have minimal or zero carbon footprint. This trend, combined with stakeholders' demand for addressing environmental issues and considerable risk of physical damage caused by climate change, puts pressure on realtors to decarbonize their ventures. As a result, Real Estate's interest in science-based targets is growing rapidly: during the last two years the number of companies engaged in the SBTi nearly quadrupled. There's good rationale for that – joining SBTi and actively working on reaching decarbonization targets makes the future of the business sounder and safer, both through keeping up with customers' expectations and by curbing climate change and its effects.

Decarbonizing a business is not an easy process. Technical difficulties aside, quantifying carbon footprint and setting up a strategy to reduce it create many challenges. To help companies with the decarbonization process, the Science Based Targets initiative (SBTi) was established. SBTi is a globally recognized organization founded as a joint venture between climate-oriented organisations – such as United Nations Global Compact and World Wide Fund for Nature – and tasked with creating standardized approach for decarbonizing companies in line with latest developments in climate science. Currently nearly 3000 companies around the world have joined the initiative, ranging from heavy industries and petrochemical sector to financial institutions and IT industry. SBTi is vital for mitigating climate changes, as it provides companies and their stakeholders with clear methodology and detailed guidance for defining decarbonization targets consistent with the Paris Agreement, thus allowing for auditing, monitoring, and revising decarbonization strategy.



1.5° C target

decarbonization strategy, that would allow to keep the global warming below 1.5° C above the pre-industrial level. To achieve that global CO₂ emissions must be cut by 48 percent by 2030 and reach net zero by 2050.



Scope 1 emission

direct emissions from owned or controlled sources, such as natural gas or transportation fuels.



Scope 2 emission

indirect emissions associated with usage of electricity, district heat, steam or district cooling.



Scope 3 emissions

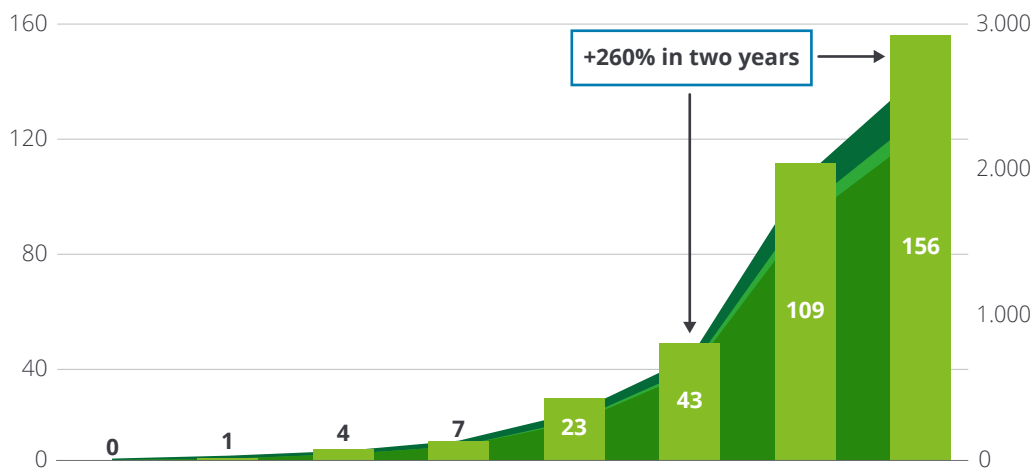
emissions outside organization’s scope 1 and 2 boundary, resulting from assets not owned or controlled by the organisation, but connected with its value chain (i.e., business travels or purchased goods).

SBTi has been experiencing extraordinary growth during the last few years: since the initiative was established in 2015, the number of participants rose from just 13 to 2940⁷. The Real Estate sector took part in this, as in the last two years, the number of companies from this sector engaged in the SBTi nearly quadrupled and currently totals 156. The combined market share of real estate companies involved in this initiative amounts to approximately 40 percent⁸. Moreover, Real Estate companies enrolled in SBTi are ahead of the curve: 61 percent of them have SBTi targets already approved – against only 46 percent of other committed SBTi participants – and out of those 72 percent decided on the most ambitious 1.5° C target, which is also above the average. Speaking of targets, Scope 3 was included by 89 percent of realtors, and in case of Scopes 1 and 2, 75 percent of companies set absolute reduction targets.

In case of sector suppliers (construction & engineering sector) and clients (companies from finance and professional services sectors) steady increase in SBTi participants can also be observed. Currently 412 companies from finance and professional services sectors, and 123 engineering and construction companies are taking part in the SBTi. Respectively 43 percent and 33 percent have targets already set. However, their ambitions differ as financial sector and professional services chose 1.5° C pathway in 86 percent of the cases, while only 63 percent of construction and engineering companies did so⁹.

It is evident, that the SBTi is gaining momentum and more companies will be joining the initiative in the future. Those companies will also be setting targets in Scope 3, which in turn will force them to look for greener suppliers, including greener options in leased spaces. This is further amplified by very active and ambitious approach of the financial and professional services sectors, which are key customers of the real estate market. A relative smaller and less ambitious approach of the engineering and construction sector may be an obstacle to reach the target, as companies active in this sector are part of Real Estate’s Scope 3 emissions.

Fig. 2 – Number of Real Estate Companies and their peers engaged in the SBTi



	2015	2016	2017	2018	2019	2020	2021	2022
Finance & Professional Services	10	21	22	38	65	104	307	412
Construction & Engineering	0	0	1	2	13	25	86	123
All others	3	12	44	98	261	598	1651	2249
Real Estate	0	1	4	7	23	43	109	156

Finding greener suppliers is not the only challenge when enforcing SBTi targets. The process is complicated and consists of several steps: calculating the baseline emissions, determining the level of ambition, setting targets and their timeline, submitting the targets to SBTi, and finally creating optimal strategy to achieve them. Calculating the baseline emissions might be difficult due to lack of actual and readily available data. Secondly, a company must set operational boundaries (up to 5% of Scope 1 & 2 emissions can be excluded from the calculations, given well-argued reason) and decide on allocating emissions between the Scopes (assuming operational control over an asset often depends on the company's decision). This determines the initial level of emissions, from which a company will be reducing its carbon footprint – set it too low and reduction targets will be hard to meet. It also determines the volume of emissions to be reduced in each of the Scopes – targets for Scope 1 and 2 must be much

stricter and ought to be met sooner than the targets for Scope 3 (i.e., targets in Scope 3 can rely on supplier engagement).

However, companies should refrain from moving as many emissions to Scope 3 as possible, as it might be disputed during an audit and counters the real effect of decarbonization efforts.

Despite those challenges, the SBTi should be viewed as an opportunity. Setting up a decarbonization target and actively working on emission reduction makes the future of the business sounder and safer – both through keeping up with customers' expectations and by curbing climate change and its effects, that can cause financial or physical damage to the enterprise. Apart from that, improved efficiency means not only less emissions, but also lower operational costs. Moreover, increased amount of data on consumed energy carriers means better understanding of the business, which can

lead to further financial savings. And looking at the aforementioned involvement of Real Estate companies in the SBTi, it seems many are well aware of those possibilities and are taking full advantage of them.

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Carbon Accounting

On the way to carbon neutrality the carbon footprint is one of the first issue to address for the real estate industry. Our ESG specialist Agustín Manzano explains the main steps on the way to the transformation to a Net-Zero economy. Undoubtedly, the time for the real estate industry to establish carbon accounting within the company is now.

Climate change is undoubtedly on the top positions of the current risk map, and our economic activities are the main cause for it.

Businesses must reduce their environmental impact, and one of the most significant ways to do this is by reducing their carbon footprint.

Regarding the real estate sector, in 2020 buildings were responsible for 37 percent of global energy-related carbon emissions¹⁰, while in the EU they amounted to 36 percent of energy-related carbon emissions¹¹.

Circa 70 percent of these emissions were related to the operation of each asset, coming from its energy consumptions¹²; however, there are also emissions associated with materials and construction processes through the whole lifecycle of the assets, generating what is called the embodied carbon. When heading for neutrality, it is essential to tackle both, operational and embodied carbon.

Taking all this into account, which should be the roadmap to address and finally reduce emissions in the real estate sector?

From our experience, the pathway towards net zero starts by carrying out an accurate and exhaustive baselining of the emissions generated by real estate entity's current construction activities and building stock to

enable them to set reduction targets. This is what is called carbon accounting.

By definition, carbon accounting is the process by which organizations measure their GHG emissions as to better understand their climate impact and therefore set goals to limit or decrease their emissions.¹³ Carbon accounting is measured within three "scopes". Scope 1 covers direct emissions from owned or controlled sources, while scope 2 covers indirect emissions from the generation of energy and finally scope 3 covers all other indirect emissions occurring in the organization's value chain.

Therefore as part of the carbon accounting process, it is essential to define whether to measure emissions directly produced by the real estate entity's own activities, or also to quantify the more difficult-to-measure indirect emissions.

Though it is considered to be somewhat of an abstract measurement, carbon accounting is hoped to provide a factual ground for carbon-related decision-making.

As a second step, a medium-term neutrality plan should be developed, with specific actions and commitments to reduce the real estate entity's emissions.

Regarding operational emissions, actions should be focused on reducing energy

demand, increasing the efficiency of the installed systems, and including as many renewable energies as possible on site. However, embodied carbon emissions must be tackled from the design phases so that they can be effectively reduced.

Considering that there are signs that specific taxes might come into force regarding entities' carbon footprint, one of the challenges the real estate sector faces is to commit to ambitious neutrality strategies that are also financially feasible. Down this road, accurate data collection and reporting, specifically carbon accounting, will play a vital role.

Even though it is a complex issue, one thing is clear: the time for entities to prepare for the reporting and reduction of their carbon emissions is now.

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Watch the
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Digital ESG Assessment for Real Estate

To achieve the targets of the Paris Climate Agreement (PCA) and reduce the carbon emissions in the real estate sector, it is essential to consider ESG criteria in real estate developments as well as in portfolio and asset management. The first step is to create transparency of consumption data in real estate projects or portfolios as well as an compliance assessment with regulatory requirements (e.g.: EU Taxonomy, CSRD, etc.), internally defined ESG targets and further ESG criteria. We provide support with our Digital ESG Assessment for Real Estate and accompany your way towards identifying and implementing specific measures designed to reduce the carbon footprint of your real estate.

Sustainability targets were defined in the PCA to reduce emissions. This led to extensive regulatory sustainability requirements (including NFRD, CSRD, EU Taxonomy) particularly for the real estate sector.

Hence, Environmental, Social and Governance (ESG) aspects have become an essential part of real estate management and should be considered throughout the entire life cycle.

Transparency regarding the consumption data, conformity with the requirements of the EU Taxonomy and other ESG criteria for individual properties as well as across the entire portfolio are key on the way to a sustainable real estate portfolio. We support you with our **Digital ESG Assessment for Real Estate**.

ESG Assessment based on regulatory requirements

Our holistic approach includes the evaluation of your real estate portfolio against the applicable technical criteria of the EU Taxonomy Regulation as well as against carefully selected criteria based on recognized regulatory frameworks, regulations and guidelines (including ECB guidelines, aspects of DGNB, LEED and BREEAM). In addition, company-specific ESG strategies (e.g. individual ESG targets, decarbonization strategy) are taken into account.

Focus on all three ESG aspects

Initially, the PCA focused on the environmental aspects. However, since properties have an impact on a wide range of stakeholders and their environment throughout its entire life cycle, it is necessary to consider social and governance aspects. Therefore, our approach is to take a holistic view of all three aspects.

Tool support

The comprehensive and holistic analysis and assessment on asset- or portfolio level is performed by using our Digital ESG Assessment Tool for Real Estate. The tool is based on the Net Zero Cloud from Salesforce in which all ESG-related data is collected, aggregated and visualized. The consumption data is converted into CO₂ equivalents by means of the stored emission factors.

The following functionalities enable efficient control of the relevant aspects for the entire real estate portfolio:

- Automated data collection (e.g.: importing invoices via optical character recognition, possibilities to connect smart meters)
- Monitoring the consumptions in real time
- Intuitive handling and transparent presentation
- Calculation of the carbon footprint
- EU Taxonomy check
- Real time tracking of changes to the ESG score and consumption after implementation of measures
- User-defined benchmarking options
- Customizable export options for integration into the Non-Financial Reporting
- GRESB score (initial assessment)
- Representation of the climate path according to Carbon Risk Real Estate Monitor (CRREM) per asset

Fig. 3 – Excerpt of our ESG Criteria/Assessment Criteria

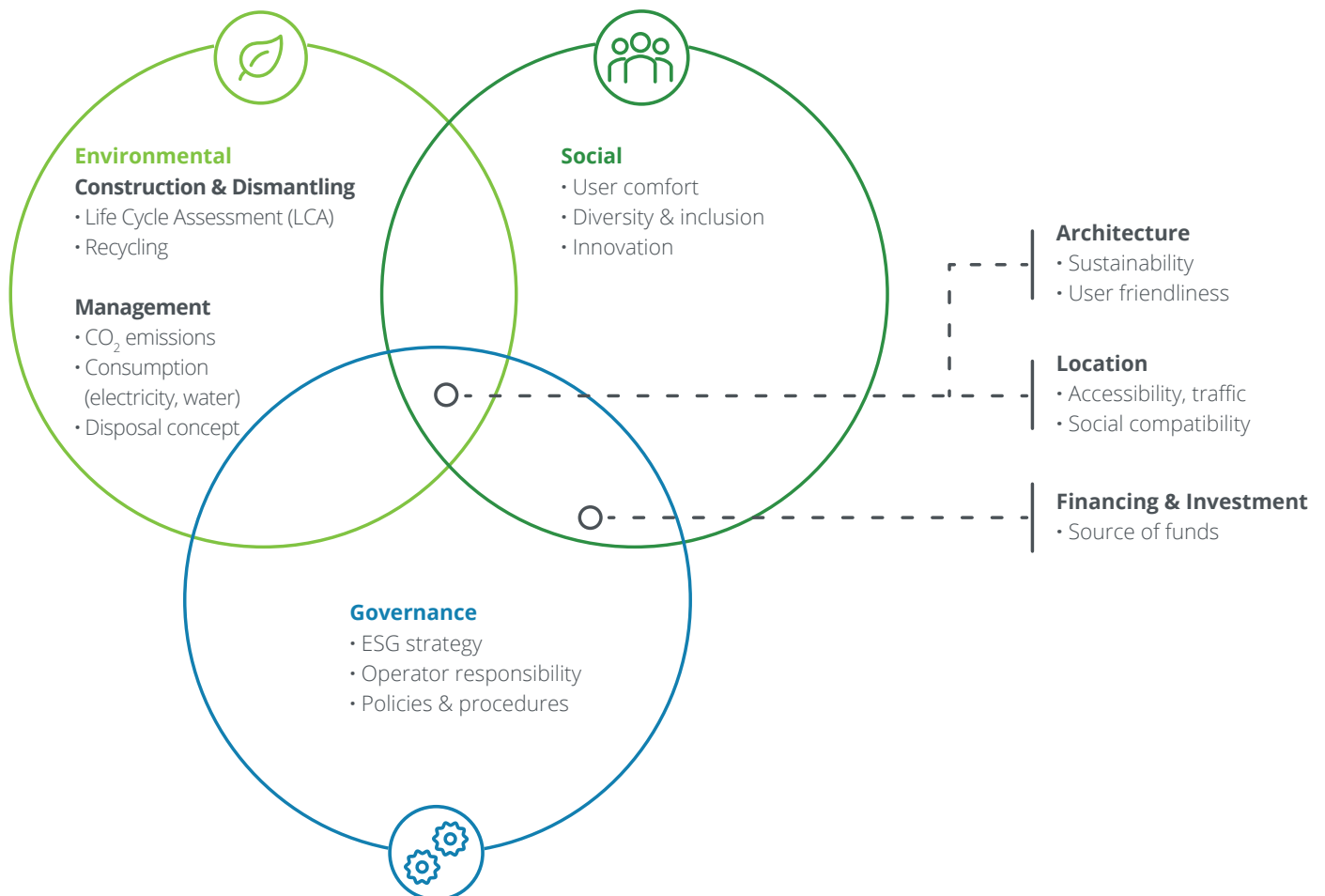
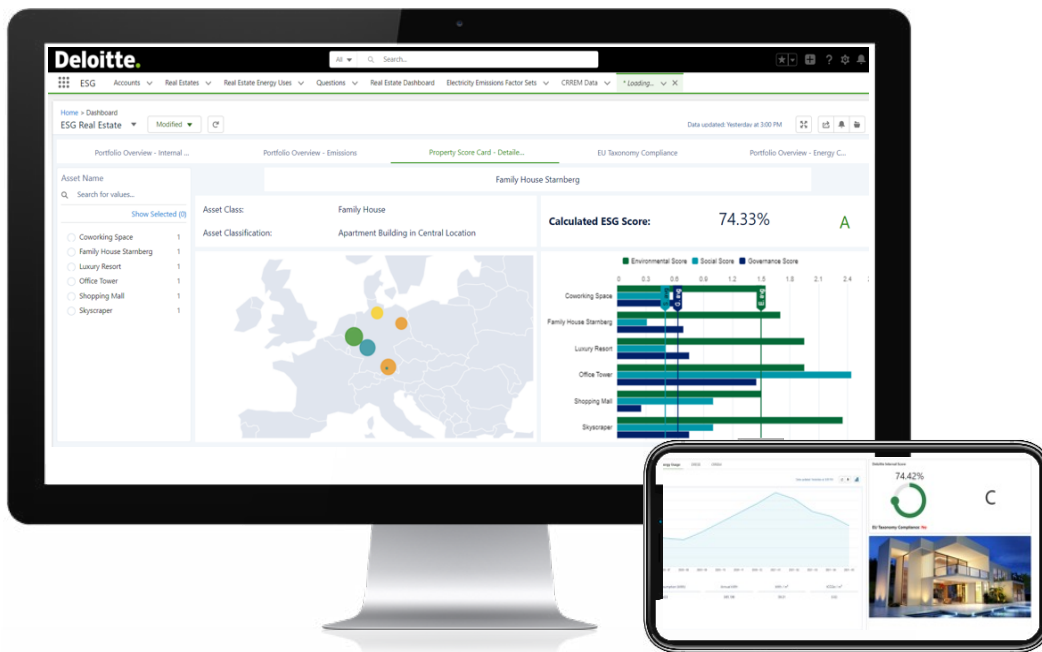


Fig. 4 – Real Time Scoring & Monitoring



Create transparency

Transparency is the foundation to continuously improve the real estate portfolio and individual properties with regard to sustainability. In our Digital ESG Assessment for Real Estate, compliance with the requirements of the EU Taxonomy Regulation and the ESG score is aggregated and presented transparently for each property and the entire real estate portfolio. In addition, the tool displays the climate path according to CRREM for each property. The point in time when the property will become a stranded asset is calculated based on the current consumption data. This allows us to identify optimization potentials early and effectively and to make them visible at a glance. Different user-defined analysis and benchmarking options are available. The assessment can be exported and integrated into any reporting format.

Identify options for action

Based on the results of the assessment a gap analysis is created which serves as the starting point for the development of specific recommendations for action. As a result, you will receive a detailed report with a clear presentation of the compliance with the EU Taxonomy requirements and the ESG scores achieved by your individual properties and across your entire real estate portfolio. Our experts work with you to develop tailored and feasible proposals for improving the ESG scores and achieving EU Taxonomy compliance for your properties. We can also support you to find partners for the implementation of the measures.

In addition to our Digital ESG Assessment Tool for Real Estate, other tools are available on the market for screening and scoring

properties and the portfolio. We cooperate with leading providers and advise on the functionalities. We will assist you in the selection of tools, collection of data and integration into the tools and the evaluation of the results.

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Sources

EU taxonomy: towards alignment

¹ companies who apply NFRD, i.e. large PIE above 500 FTE.

² resource.html (europa.eu)

³ resource.html (europa.eu)

⁴ Deloitte has developed a tool to address the issue of risk assessment linked to climate change called Climwise.

⁵ Annex to the platform on Sustainable Finance's report with recommendations on technical screening criteria for the four remaining environmental objectives of the dssjijuw

SBTi: decarbonizing real estate in line with climate science

⁶ „Zerowy Ślad Węglowy Budownictwa – Mapa drogowa dekarbonizacji budownictwa do roku 2050”, Polish Green Building Council, June 2021, page 4.

⁷ sciencebasedtargets.org/companies-taking-action (as of May 10th 2022).

⁸ Calculated as sum of reported annual

revenue of Real Estate companies

engaged in the SBTi, divided by value of global Real Estate market, which was based on the report “Real Estate Market Size, Share & Trends Analysis Report By Property”, Grand View Research, 2022.

⁹ sciencebasedtargets.org/companies-taking-action (as of May 10th 2022)

Carbon Accounting

¹⁰ 2021 Global Status Report for Buildings and Construction, developed by Global Alliance for Buildings and Construction for the UN Environment Programme.

¹¹ EU to Start Measuring “Embodied” Carbon Emissions from Buildings, <https://www.eceee.org/all-news/news/eu-to-start-measuring-embodied-carbon-emissions-from-buildings/>.

¹² “Whole-Life Carbon: Challenges and Solutions for Highly Efficient and Climate-Neutral Buildings > BPIE – Buildings Performance Institute Europe.” BPIE, 28 June 2021, <https://www.bpie.eu/publication/whole-life-carbon-challenges-and-solutions-for-highly-efficient-and-climate-neutral-buildings/>.

¹³ “Carbon Accounting 101.” Supply Chain Solutions Center, www.supplychain.edf.org/resources/carbon-accounting



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