WHEN WHOLE FOODS Market began to expand its footprint by rolling out stores in the early 2000s that garnered the U.S. Green Building Council’s LEED (Leadership in Energy and Environmental Design) certification, it encountered a dilemma: few shopping center developers shared its commitment to sustainability.

These days, the supermarket chain is finding an eager partner in some developers. “Over the last three to four years, some real estate developers are coming to us and indicating that they want to pursue LEED certification for their centers,” says Kathy Loftus, Whole Foods’ global leader of sustainable engineering and energy management.

Shopping center owners and landlords, she says, have caught on to the benefits of going green, which in the past many viewed as too costly and complex. At the forefront of this transition, a number of retail REITs have made sustainability an integral part of their corporate social responsibility platforms, although their focus in recent years has shifted largely from green building to improving existing properties. In many cases, landlords are experimenting with energy conservation programs and other initiatives at a handful of centers and expanding only on those that make financial sense.

ONLINE AND ADVANTAGED
Like some of their largest tenants, retail REITs have found that sustainability programs not only improve their public images but have more tangible benefits, ranging from faster entitlement, particularly in tightly regulated U.S. coastal markets, to cost savings. “If you are building in California, where it can take four years to get permitted, having a green commitment will give you greater certainty,” says Jerry Yudelson, founder of Yudelson Associates, a consulting firm specializing in sustainability planning and green building.

Developers “often compete with one another in the planning stages. If you can get online faster, that is an advantage,” adds Yudelson, who worked with Regency Centers Corp. (NYSE: REG) in 2007 to craft its approach to sustainability.

Over the past five years, Regency has seen many cities take a much greater interest in green building, and the company has become more adept at navigating the LEED certification process. Since 2009, about 80 percent of its projects, including redevelopments, have achieved or are seeking LEED certification, according to the company.

“We’ve gotten better and more efficient at certifying our projects. We believe this experience is a competitive advantage because so many municipalities or other stakeholders are interested in green buildings,” says Mark Peternell, Regency’s vice president of sustainability.

Regency’s environmental focus helped it secure the rezoning it needed to develop the Market at Colonnade in Raleigh, N.C. The LEED-certified center was one of only four new retail developments to open in the Research Triangle last year, according to Regency. It is anchored by a LEED-certified Whole Foods Market and features a stormwater management system that captures runoff in underground cisterns. The non-potable water is used within Whole Foods and to irrigate the site.

At various centers, Regency has implemented energy and water conservation measures that have reduced related expenses by more than $1.3 million cumulatively over the past three years. At nearly 100 centers, it installed “smart” irrigation controllers that adjust the frequency and duration of watering based on local weather conditions. The company’s conservation measures have resulted in lower common-area maintenance charges for tenants and reduced operating expenses for Regency, according to Peternell.

“I think we have proven we can do the right thing while improving the bottom line,” he says.

A GREENER CONSUMER
As part of their energy conservation strategies, both Regency and Simon Property Group Inc. (NYSE: SPG) are encouraging the use of electric vehicles among shoppers. Last year, Simon launched a program to install self-service, electric-vehicle (EV) charging stations at its malls, making it among the first retail REITs in the country to do
so. The Indianapolis-based company, which will collect a nominal fee from users after a free introductory period, kicked off the program at Florida Mall in Orlando and at Stanford Shopping Center in Palo Alto, Calif.

Earlier this year, Regency announced that it is installing EV charging stations at 19 centers in Arizona, California, Oregon, Tennessee, Texas and Washington D.C. Through the pilot program, Regency is participating in a $230 million, public-private project, funded in part by the U.S. Department of Energy, that is deploying charging stations in metro areas throughout the United States and collecting EV usage data.

Managed by San Francisco-based ECOtality Inc., the EV Project is also evaluating revenue-generating systems for commercial and public charging stations. Regency plans to install chargers at additional centers if its pilot demonstrates that it makes financial sense to do so, and there is sufficient consumer demand, says Peternell.

High gas prices and an increased environmental awareness among consumers are expected to continue to push up demand for electric vehicles.

THE WAL-MART FACTOR
The growing interest in sustainability among retail REITs is also closely tied to an increased environmental awareness among some major tenants, particularly grocery chains and mass merchants, including Wal-Mart Stores Inc., the world’s largest retailer. Such tenants, which operate on slim margins and consume enormous amounts of electricity, are motivated partly by a desire to curb utility and other operating costs, observers say.

The prevalence of triple-net leases in the sector means that the majority of operating costs is passed along to tenants. However, landlords may have “unrecoverable” expenses associated with maintaining vacant space or due to caps on tenants’ common-area maintenance charges.

“So, the large publicly traded retail tenants are the ones that are forcing more sustainable features in buildings and more efficient management,” says Norman Miller, a real estate economist and professor at the University of San Diego.

Nonetheless, the retail real estate sector still has a long way to go before LEED-certified buildings are commonplace, according to Miller. He estimates that fewer than 1 percent of all U.S. retail properties are LEED-certified, versus about 5 percent of office buildings.

In the office sector, many tenants pay a flat rental fee that includes utilities, giving landlords a strong incentive to reduce energy and waste costs. Office REITs also view green buildings as a competitive advantage in attracting corporate and government tenants, Miller says.

“We are now at the point where people in the retail sector have enough experience with green building that costs have come down, and there is more pressure on the tenant side,” he explains.

UNCOVERING NEW OPPORTUNITIES
With development at extremely low levels, retail REITs are spending far less time focused on green building than they were prior to the Great Recession. In most cases, their sustainability efforts are aimed at improving the performance of existing properties on a number of fronts, particularly energy efficiency. Some landlords are even finding ways to generate income on their initiatives.

“Sustainability is one of the lenses we can use to look at our existing portfolio and uncover new opportunities for improved profitability,” says Will Teichman, Kimco Realty Corp.’s (NYSE: KIM) director of sustainability.

Formerly a member of Target Corp.’s sustainability team, Teichman joined Kimco in early 2011 and has since devoted a portion of his time to expanding the company’s efforts to produce clean energy at its centers. Those efforts, he says,
**SECTOR SPOTLIGHT**

have benefitted from a sharp decline recently in the price of solar panels.

So far, Kimco has installed rooftop solar systems at six centers in New Jersey. The systems supply lower-cost energy to several tenants at each property, and Kimco generates income on the sale of the power. It also collects income on the sale of renewable energy certificates under a state incentive program, although the so-called REC market has seen price fluctuations recently.

At Kimco, green initiatives must compete for capital with other potential investments by demonstrating their return potential, Teichman notes. “The most sustainable way to become a more sustainable business,” he says, “is to align these programs with the underlying interests of the business.”

“**We can’t control tenant improvements, but if we are going to give them a tenant allowance, we’d like to see it invested in a way that is sustainable,”** he says.

Thanks to the “green box” program, a 40,000-square-foot addition to Bethesda Row, a mixed-use center in Bethesda, Md., owned by Federal Realty, received LEED gold certification last year. A key tenant in the space, Equinox fitness club, has received LEED silver certification.

The center’s sustainability efforts include a recycling program that turns oil and grease waste from its restaurants into biofuel.

The program is just one of the many ways landlords are collaborating with tenants to create more environmental friendly centers. Approaches vary from region to region and are influenced by factors including government incentives for solar power and energy prices.

Landlords still face plenty of challenges too, including an absence of widely accepted, sector-specific benchmarks for energy efficiency. The Environmental Protection Agency’s Energy Star ratings, which are commonly used in the office sector, aren’t applicable to shopping centers because it is difficult to gauge the total energy consumption of multiple users, says Joe Jaworski, vice president of national operations for the U.S. unit of the Sydney, Australia-based Westfield Group (ASX: WDC).

Jaworski is working through the International Council of Shopping Centers to devise a Web-based tool for scoring the energy efficiency of shopping centers, which has long been a key concern for Westfield.

In the U.S., Westfield has implemented a proprietary, enterprise energy-management system called ecoWISE. Designed to maximize operational efficiency, the Web-based system allows Westfield to monitor, in real time, all devices at its malls that use power, pinpoint any problems and make changes remotely. Air conditioning and lighting systems, for instance, can be programmed to automatically adjust for actual local conditions, such as outdoor temperatures and natural-lighting levels. Westfield expects to reap at least 5 percent annual energy savings at each property and is rolling out ecoWISE in Australia.

“It used to be that being green was simply philanthropic,” says Jaworski. But as a public company “we have shareholders and an obligation to provide them with a return. So everything we do has a pro forma.”

Anna Robaton is a regular contributor to REIT magazine.