



BUILDING GREEN

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THE LEGAL RISK IN “BUILDING GREEN”: NEW WINE IN OLD BOTTLES? A USGBC Panel Discussion

INTRODUCTION

Conjecture, anecdote, and even rumor swirl around recent presentations, workshops and discussions, circling the question of what legal claims may be based on the design, development and construction of sustainable buildings. To construct a realistic appraisal underlying these concepts, USGBC convened a small working group of four attorneys who are leaders in the green building legal community and who are familiar with and supportive of LEED® certification. Dan Slone (McGuire Woods LLP), Keith McGlamery (Ballard Spahr Andrews & Ingersoll, LLP), David Blake (Seyfarth Shaw), and Jeff York (HOK) volunteered to share their informed insights. Each attorney serves as legal representative to stakeholders in a least one segment of the building industry, including architects, designers, developers, tenants, owners, contractors and subcontractors. USGBC asked the members of the group to engage in a discussion of what new legal theories have been advanced in the context of green buildings.

Many commentators have warned of green building litigation involving fraud, negligence, breach of contract, and violations of federal, state and local regulations. The members of the working group generally agreed that such risks are nothing new. All persons involved in building development, design and construction face such risks if there are false claims, lack of due care, failure to meet obligations, or deceptive marketing. Sustainable building projects are not exempt from such concerns. In the conversation that follows, we asked each attorney to sketch out possible risks for green building projects and ways in which to mitigate them. Perhaps surprisingly in light of the increased attention in seminars and workshops noted above, much of the discussion among the attorneys suggests that many of the legal theories advanced in those venues to suggest novel liability associated with building green are, instead, simply new wine in old bottles.

I. IS THERE NEW LEGAL EXPOSURE FOR GREEN BUILDING?

USGBC: Does the real estate community face new potential liabilities by building green?

Mr. McGlamery: The framework of legal liability is not new. However, some of the claims within that framework are new or, at least, less familiar. For example, local building codes and land use regulations are an accepted part of the legal landscape for real estate owners. A new variation, however, is the requirement of LEED certification for public and, in some instances, private buildings within the local jurisdiction. As another example, owners generally have an awareness of the types of disputes that can arise with contractors and architects. What is new is allocation of responsibility among the members of the project team party for obtaining LEED certification and the extent of the liability each bears for failure to obtain that certification.

Mr. Slone: A developer overseeing a spec building falls between the roles of contractor and owner, and as such, accounts for the risks of several actors, including lender, prospective owner, and future tenants. For years the building industry has incorporated risks associated with plumbing, electricity, HVAC systems, and significant

structural risks related with ever-taller buildings. Contemporary green building is relatively young, with new approaches and new technologies. The specific risk issues to be addressed as green building matures center around expectations, regulation, and new technology. The industry must fold new challenges into existing risk management mechanisms--but green building is not a new paradigm of risk beyond management.

Mr. York: According to insurance professionals HOK has consulted and my own experience, there have been very few claims arising out of sustainable design to date, despite concerns to the contrary. The risks to architects in “building green” are essentially the same as the risks on other projects; architects are expected to perform with the skill and care ordinarily provided by other architects in the same or similar circumstances. In the green setting, however, this standard takes on a different angle for a few reasons. The “reasonable architect” standard looks to other architects in the same or similar circumstances and what they would have done on a project of the same size, scope and complexity. Defining who falls into this pool becomes slightly more involved: do you look at other LEED Accredited Professionals? Or do you look to architects that have a certain level of experience in designing green? The answer is “probably”, but is very fact-dependent.

II. WHAT ARE THE REGULATORY CONCERNS?

USGBC: What are some examples of regulatory compliance issues confronting contractors?

Mr. Blake: A question contractors wonder about is whether they are responsible for complying with green regulations. Numerous states, counties, cities and towns across the country have adopted regulations that require varying levels of LEED compliance for public, private, or public and private construction. For example, in Washington DC, all privately owned, non-residential projects of at least 50,000 gross square feet for which the first construction permit application is submitted after January 1, 2012 must be certified at the LEED Certified level. Is the contractor liable if a project does not comply with one of these green regulations?

Mr. Slone: It is critical that developers stay apprised of regulatory requirements. As David noted, many cities and states have already adopted green building codes and regulations—many of which incorporate LEED standards. As the industry and regulations evolve, prudence is necessary to maintain regulatory compliance and avoid associated risk. As an example, terms like “green” and “sustainable” are not clearly defined and may create conflicting expectations between parties. Established construction terms of art such as “substantial completion” also may need new clarification with regard to green building. Ongoing efforts to clarify terminology will help. The Federal Trade Commission is reviewing its “Guides For the Use of Environmental Market Claims,” or Green Guides (16 C.F.R. 260), with a particular focus on the perception and substantiation of green claims related to buildings.

Mr. McGlamery: Part of the FTC’s mission is dealing with unfair or deceptive trade practices affecting consumers. The standard followed by the FTC is that those making express or implied claims about the attributes of their product or service must have a reasonable basis for their claims at the time they make them. The FTC’s view with regard to “environmental advertising” is that a reasonable basis often requires

competent and reliable scientific evidence. An example of where this might arise is in the area of heightened expectations about improved health conditions for occupants of green buildings, such as apartments or condominium units.

USGBC: Should this be a big concern for homebuilders or others dealing with consumers?

Mr. McGlamery: FTC rulemaking in this area may create what I would expect to be a temporary heightened anxiety and confusion among those involved in sales or leasing of residential real estate. However, I don't think this will significantly alter the way the vast majority of homebuilders conduct business because they are already accustomed to compliance with state consumer protection laws concerning false and misleading advertising and marketing.

III. THE INCREASED CONCERN ABOUT ACHIEVING LEED CERTIFICATION.

USGBC: A concern being expressed by many commentators relates to achieving, or failing to achieve, LEED Certification. Is this a concern of the clients with whom you work?

Mr. Blake: Yes. One fear shared by contractors and subcontractors is that the project they are building will not be certified at the level stated in the contract. For example, what happens if the contract states that the contractor is responsible for the project achieving a certain level of certification, such as LEED Gold, but USGBC certifies the project at the lower Silver level, or not at all? Currently, there are no reported cases that have addressed this issue. However, there are well established legal principles concerning design and performance specifications that likely will control the outcome. On the one hand, design specifications describe in detail how the project is to be constructed, and contractors are to follow them like a road map. In contrast, performance specifications set forth objectives to be achieved and leave it to the contractor to determine how to build the project to achieve those objectives. Providing a contractor with a detailed set of plans and specifications it is required to follow, but also telling the contractor it is responsible for achieving a certain level of LEED certification, constitutes a mixing of design and performance specifications. Courts have addressed this issue in other contexts and have found that the contractor is not responsible for achieving the specified objective. Accordingly, as in most projects, if a contractor is provided with a set of detailed plans and specifications and it follows them, it should not be liable for the results that are achieved or not achieved (in this case, a specific level of LEED certification).

Mr. McGlamery: Failure to obtain a particular level of LEED certification, depending on the circumstances of a particular project, is a significant concern of project owners, not only if the LEED certification level is required by local law, but also if it is required by a tenant or other end-user. If the LEED certification is required in a lease or build-to-suit contract, the owner faces the potential loss of a tenant or sale as part of, or in addition to, a breach of contract claim for damages.

Mr. York: From an architect's perspective, or more specifically, from the perspective of legal counsel representing an architect in contract drafting, the biggest concern is not to guarantee a certain level of LEED certification. There are just too many factors that go into certification for the architect to be able to guarantee a certification level.

Decisions made by the building's owner, actions taken by the contractor and post-occupancy usage are all out of the control of the architect-- and all affect various LEED credits.

Mr. Slone: Yes, expectations of, and reliance on, a certain LEED certification level can cause conflict. Consider the Maryland case of Shaw Development v. Southern Builders. As part of a condominium project, Shaw planned on funds from Maryland's green building tax credit program, a program limited to qualifying LEED projects and restricted to a set window of time. The project did not have LEED qualification within the window of time and Shaw sued for damages for the loss of tax credits, among other claims.

IV. NEW PRODUCTS AND TECHNOLOGY AS RISK CONCERNS.

USGBC: Several of you have referred to challenges of new products and new methods and Dan referred to new technology as a risk issue. David, how does that play out for contractors?

Mr. Blake: For contractors particularly, there are time sensitive components of green projects that have the potential to cause delays. Some green products are in high demand and low supply, which results in long lead times. Additionally, there are processes on green projects, such as the two-week flush-out of the HVAC system prior to occupancy, that may add time to the overall construction period. If a contractor neglects to include this and other green activities in the project schedule, critical path delays may result. Once a contractor becomes familiar with these activities, much of the risk can be removed by inputting them into the CPM schedule and then managing the schedule.

USGBC: Jeff, address this concern for architects, and Dan, share some thoughts from the developer's viewpoint.

Mr. York: There are a lot of untested "green" products in the marketplace that do not have reliable performance data. This, of course, is a risk faced on conventional projects that utilize new products, but on a "green project", owners are often looking for the untested materials to provide more significant returns in terms of performance (heating, cooling costs, etc.). When these untested products fail to meet the expected levels of performance, the "cost" to owners may be higher than on a conventional project.

Mr. Slone: From a developer's perspective, innovative green technologies raise issues of risk allocation. Who is responsible for the integrity of a new green roof design or innovative gray-water system or experimental insulation material? If the glass windows that are already ordered and installed lack the necessary insulation qualities, who pays? These specific risk issues must be addressed as green building moves forward.

V. MINIMIZING RISK OF LEGAL LIABILITY: KNOWLEDGE AND EXPERIENCE

USGBC: It is clear from what each of you have said that there are legitimate concerns. So, if you would, please share your thoughts about some of the ways the risks can be

addressed. To begin this part of the discussion, we have noted that many of those speaking and writing about green building emphasize the importance of knowledge and experience of the project team. Assuming you agree with those emphases, can you cite some examples?

Mr. McGlamery: Obviously, knowledge and experience are key. On the design side, ignorance of LEED prerequisites can be costly to all concerned. On the construction side, it may be necessary to explain to a new painting subcontractor why low VOC paints were specified and why substituting a high VOC paint, even though it is a color match, is not acceptable. Also critical is that the management and supervision of the project be done by someone with a thorough understanding of LEED credits.

Mr. Blake: One of the biggest risks a contractor faces on any project is submitting a bid without fully understanding its obligations. This is especially true in the area of green construction, where many contractors are still learning the particular means and methods associated with these projects. Fortunately, contractors can manage this risk by carefully reviewing the bid package documents before submitting their bid and signing a contract. By carefully reviewing the bid package documents, contractors can identify the green activities they need to perform, estimate the risks and cost of the same, and submit a bid that properly covers these activities and risks.

Mr. York: At the end of the day, the risks are of the same type on green projects as they are on conventional projects, but of a different degree. The architect is expected to use professional judgment in performing his or her services. This is the same as it has always been. Problems arise when there are unrealistic expectations and a lack of education with regards to the certification process on the part of the various parties to a project. From this perspective, the greatest risk management tool is reaching understanding and clear communication between the architect, owner and contractor.

VI MINIMIZING RISK OF LEGAL LIABILITY: CONTRACTS

USGBC: In addition to knowledge and experience, several of you have mentioned the importance of contracts or particular contract provisions. Please expand on your thoughts on the importance of contracts in managing risk in green building projects.

Mr. Slone: Much of the risk associated with green building may be remedied with precise, uniquely-tailored contractual language. An appropriate contract can clearly define vague terms, exactly delineate performance and/or certification expectations, and explicitly allocate any risks of new technology. While some commentators recommend avoiding guarantees, a precise contract can appropriately define the guarantee and mitigate risk. Indeed, a contractual provision to attain a certain LEED certification creates a clear liability—qualitatively (LEED Gold, for example) and temporally (one-time certification, rather than ongoing performance standards). Moreover, risk may be limited contractually with liquidated damages and limits on corrective work, and a contract can address issues that may arise from design or construction alterations that adversely affect the building's overall performance.

Mr. McGlamery: A fundamental risk management tool is the use of a clearly defined scope of work in construction contracts. In building green, it may mean specifying the relationship between LEED credits and specific project components in the scope of work for the architect and contractors. Such an approach emphasizes the importance

of LEED specific matters and it can also be part of allocating responsibility for obtaining a particular level of LEED certification.

Mr. Blake: Some contracts are prepared so that the contractor is responsible for the project achieving a certain level of LEED certification. If the architect did not design the project to satisfy the prerequisites or the required number of credits for certification at a particular level, it would not be reasonable to hold the contractor liable for the project not being certified. Accordingly, a clause imposing blanket liability on the contractor for achieving certification should be deleted.

Another way that contractors can mitigate risks for potential damages is through a liquidated damages clause. A liquidated damages clause specifies a specific and predetermined amount of damages to be paid in the event of a breach in lieu of the aggrieved party recovering its actual damages. A contractor could structure a liquidated damages clause to cap the contractor's potential exposure for the types of "green damages" discussed above and thereby provide it with a level of certainty concerning the same.

Additionally, many of the potential green damages owners might incur could be imposed as consequential damages. Contracts sometimes include a "waiver of consequential damages" clause that prevents the owner and contractor from recovering consequential damages from each other in the event of a breach. A contractor could shield itself from certain types of green damages through the inclusion of such a clause in its contract. Given the potential protection they offer, contractors should think twice before agreeing to delete these clauses on a green project.

VII. MINIMIZING RISK OF LEGAL LIABILITY: A FEW ADDITIONAL IDEAS

USGBC: Are there other risk management strategies available that haven't yet been discussed?

Mr. Blake: Contractors can manage their obligations through several document control techniques, including use of a Quality Control/ Quality Assurance Plan, a LEED Action Plan, and a Credit Management Spreadsheet. The Quality Control/Quality Assurance Plan should be specific to the job, should incorporate green activities, and should clearly identify who performs the various quality control/assurance activities, such as third party testing. The LEED Action Plan is used to define the credits that the contractor or subcontractor is required to actively manage, as well as how it will manage those credits. The Credit Management Spreadsheet is used to calculate the progress that is being made toward each specific credit.

Mr. Slone: Luckily, existing mechanisms of risk mitigation—including management practices, insurance, and contractual provisions—can effectively address green building risks, just as they've addressed risks associated with previous building technologies. Pre- and post-construction management and operations may include: avoidance of overreaching in marketing and representations; test-construction to evaluate a new technology; performance testing of systems; field inspections for proper installation; and walkthroughs, written manuals, and purchaser orientation for proper operation and maintenance. Qualified professionals can advise on such management and monitor regulatory compliance. Notably, insurers have begun adding green building endorsements to builder's risk products, aimed to mitigate builders' potential

financial risk associated with changes in environmental standards, repairs using green materials, additional debris-removal expenses, and loss of tax credits.

CONCLUSION

All members of the task force agreed that the ways to manage legal risk with green building projects, and specifically those seeking LEED certification, are fundamentally the same ways professionals in the real estate and construction industry have always managed legal risk, in basic ways. Highlighted by the panel was the combination of creating realistic expectations, clearly defining scope of work, and maintaining quality project supervision. The most effective protection against legal risk, whether contract, regulatory or other, is the combination of knowledge and experience.

USGBC is grateful for the insights and wisdom offered by these legal advisors. Clarity, shared expectations, and appropriate planning—the usual tools in risk management—are more important than ever in sustaining the green building industry. As green building matures, it is likely that risks involved in “building green” will be just another risk undertaken by informed professionals in the industry.

Members of the USGBC Legal Working Group

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Keith W. McGlamery is a partner in the Real Estate Department of the Washington, D.C. office of Ballard Spahr Andrews & Ingersoll, LLP. He represents clients in the acquisition, development, financing, leasing, management, and disposition of commercial real estate. As one of the small number of lawyers in the United States who is also a LEED® Accredited Professional, he advises clients on a variety of legal issues related to green building. Mr. McGlamery earned his B.A. degree from Oklahoma State University and his J.D. degree from the University of Wisconsin Law School.

Dan Slone is a partner in the Richmond, Virginia office of McGuireWoods LLP. He represents developers and localities in creating innovative and sustainable codes and contracts for large-scale projects throughout the United States. Mr. Slone also represents green builders, manufacturers of green products, architects, and other professionals advancing green designs. He has represented USGBC for almost a decade and has been national counsel for the Congress for the New Urbanism and the World Green Building Council since their creation. He is on the boards of Greenroofs for Healthy Cities, Greening America, Bioregional North America, the Form-Based Codes Institute and the National Charrette Institute, among others. Mr. Slone speaks nationally on a wide array of subjects, including liability for green projects,

and Wiley recently published the book he coauthored with Doris Goldstein entitled A Legal Guide to Urban and Sustainable Development for Planners, Developers and Architects.

Jeff York is an in-house attorney at the architecture firm HOK. At HOK, Mr. York drafts, reviews, and negotiates contracts for projects of all sizes and uses around the world, as well as handles other corporate matters. He has taken on the role of advising HOK on the risks and legal issues associated with building green, sustainable design and contracting for providing LEED services. Mr. York received his J.D. and M.B.A. from Washington University in St. Louis where he was a member of the Washington University Journal of Law and Policy. Prior to working at HOK, Mr. York was in private practice where he focused on construction litigation.

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