Memo to: **John Kenward**
From: **Legal**
Date: **February 28, 2008**
Re: **Background Materials on Liability and "Green Buildings"**

The following are excerpts from Internet materials about liability and "green buildings". Although many references are to the liability of architects and other professional advisors, most apply just as easily to contractors.

Website: *Greenbuildings NYC*
Green Construction Law: As Legislation Proliferates and Insurance Issues Emerge, Is Green Building's Future Being Compromised? by Stephen Del Percio
If state and local governments continue to enact green building ordinances, regardless of whether they're in the form of mandates or incentives, or applicable to public or private projects, we may be laying the groundwork for some nefarious consequences. Private owners may simply refuse to proceed with LEED projects and choose to build elsewhere because there would be no assurance that the project's designers were backed by adequate coverage in the event that the project did not achieve the certification.

Currently, there's no insurance product on the market that provides an endorsement to a professional liability policy and expressly articulates coverage for this type of scenario.

Federal Building in San Francisco. Essentially, despite the project touting itself as a high performance building, it did not even achieve a LEED Certified level- significant because of a GSA mandate for federal buildings to reach that level of certification. Mayne stated that he "wasn't arrogant, but . . . was confident. I just assumed we had the Platinum rating . . . all along we went through LEED and it wasn't working. . . . It's just very prescriptive . . . you either operate under that or you don't." Mr. Koerner suggests that Mayne and his firm may be trying to cover their tails by suggesting that LEED itself- and not the process by which they designed their building- is flawed. Could this be a high-profile example of a green project team recognizing its own potential liability and setting itself up for a pending litigation?

Rather than quickly legislating individual rating systems into code, policymakers would be better served by directing their efforts at analyzing how risk could be more effectively distributed amongst stakeholders. Otherwise, some of these potential outcomes could soon become a frightening, and unwelcome, reality.

LEED-AP Designation Not Just for A/E/C
by Stephen Del Percio, October 2nd, 2007
Crain's perceives the legal industry as recognizing the risks associated with the LEED rating system. It refers to one attorney who has "been studying for the accreditation test because the environmental standards could lead to new types of litigation. He foresees disputes over whether new buildings actually meet the environmental codes and who is responsible if they do not."

Another Green Perspective, by Ann Whitaker

> Unless the granting of the LEED rating is taken away from a private agency (not accountable to anyone) and given to the building department, I think the city is asking for trouble. The LEED rating is not enforceable, the criteria change regularly, and points can be awarded (or not awarded) seemingly on a whim by USGBC.

Green Insurance Law: Industry Thoughts on BIM and LEED Coverage for Design Professionals,
by Stephen Del Percio, December 11th, 2007
Zurich's panelist rather ominously observed that his firm has "never seen a standard of care shift so quickly with so much media coverage and political backing." He also noted that adding fuel to the sea change are owners who are "being told that sustainable design will help save them money. Claims start with violated expectations." Insurance against professional negligence protects design professionals against claims that they did not perform up to their standard of care, which is defined as the level of skill of similar professionals in a similar location. For example, similar professionals could be deemed to be LEED Accredited Professionals, expected to design projects and building systems that perform at a higher level. The danger here is that all architects and engineers- whether they are competent in green design practices or not- will be held to that elevated standard of care. If their designs do not perform as intended, or do not incorporate sufficient sustainable measures, it is possible that litigation could ensue.

Green Business Law: Need for Green Counsel Becoming Increasingly Salient as Green Claims are Brought Against Design Professionals,
by Stephen Del Percio, June 19th, 2007
I've written before about the potential for design professionals to unwittingly expose themselves to unanticipated risks on green construction projects. In a presentation at last month's 2007 AIA National Convention in San Antonio, Frank Musica, an attorney with a Maryland-based insurance company, provided an overview of twenty-one actual "green claims" brought against engineers and architects. A copy of his PowerPoint presentation is available for download here.

The claims range in size and scope, from a project failing to achieve the level of LEED certification at which the owner marketed it, to a fascinating scenario where the architect specified a (seemingly) innovative exterior solar shading system that turned out to be patented. The owner sued the architect in negligence for not researching whether the system was covered by an enforceable patent and to demand contractual indemnification for intellectual property infringement damages. Other scenarios that Musica described in his presentation involve:

- A school district which brought suit against a design team where energy use on a purportedly sustainable, three school project that included commissioning services failed to "reduce operating costs by fifty percent" over comparably-sized schools as stated in the design team's contract;
- A homeowner retained an architect for an addition with the goal of improving indoor air quality and reducing energy costs through green design. The architect apparently sold the client on its green expertise and ability to deliver the project within the specified budget. The

owner was unhappy with the finished product and sued the architect under the appropriate consumer protection law, claiming fraud in the inducement of the contract and seeking its recission;

- An architect was "impressed" with promotional materials from a green product manufacturer and the owner agreed to use it on the project. However, the product was not readily in stock and project delays ensued. The owner sued the architect on the grounds that the delays stemmed from its failure to inform the owner that delayed delivery was possibility; and
- A variety of other claims involving guarantees of indoor air quality levels, a cork flooring system specification that nevertheless resulted in water retention and a subsequent mold problem, and a dispute over responsibility for the recycling of construction debris as mandated by the local municipality.

Green business risks are real but largely unexplored. What strikes me is that these are actual claims that architects have tendered to their insurance carriers, not pontification from some legal scholar. While we're still waiting for a court to issue an opinion arising out of a green litigation, it's clear that design professionals- and indeed all construction project stakeholders- must consider all of a green project's ramifications when negotiating their contracts or even weighing whether to participate on the job in the first place. For example, Musica recommends that design professionals carefully specify sustainable products by demanding technical data from manufacturers- not promotional materials- and keep their clients informed of any risks that they uncover as they perform their green due diligence. Finally, seeking advice from counsel familiar with green building rating systems and the risks that sustainability presents is an absolute imperative- no matter the business context- particularly given that green continues to rapidly penetrate an increasing number of industry sectors.

Is LEED Legislation- Whether Public or Private- Undemocratic?
By Stephen Del Percio, August 8th, 2007
In an article written earlier this week, Dan Walters, a columnist at the Sacramento Bee, articulated his concerns over a LEED-driven green public building regulatory scheme by calling such legislation "part of a broader legislative tendency to avoid tough policy decisions by shifting them to unaccountable outside organizations." Walters was writing with respect to California's Senate Bill 86, which would require public projects to comply with LEED beginning on January 1, 2009. Although Walters acknowledged that USGBC is "a legitimate organization that acts as a forum for agreements on environmentally friendly building standards," he also noted that means by which it has- and continues to develop- the LEED standards are promulgated by its own membership base and internal policies.

Walters calls Bill 86 a "two-pronged assault on democratic process that not only bypasses the usual procedure for making new law, but also transfers the regulations authorized by the new law to a private organization that's completely unaccountable to the public." As I have similarly observed here at gbNYC previously, Walters also pointed out that should Bill 86 pass, Californians will be "on the hook for whatever standards USGBC developed by whatever process it uses." (This point is obviously well-taken, but it should be pointed out that USGBC does solicit input from its members and member organizations during the public comment periods prior to introducing new rating systems. Of course, the rejoinder here is that the commenting and pilot periods take too long to finally implement and either discourage potential applicants or encourage standards-adopting organizations to create their own standards rather than waiting on USGBC.) Walters' piece did not

address the LEED creep scenario (LEED mandates applying to private projects) but his concerns certainly resonate in that context as well.

Surety Industry Raises Red Flags Over D.C. Green Building Act,
by Stephen Del Percio, October 11th, 2007
Concerns over LEED creep (the application of LEED mandates to private projects) include the potential for awkwardly- or hastily-drafted legislation to change the risk structure associated with a given green construction project for various project stakeholders. For example, back in early August, the Surety and Fidelity Association of America ("SFAA") and the National Association of Surety Bond Producers ("NASBP"), which collectively represent the surety companies that underwrite most of the surety bonds that are issued on construction projects in the United States, wrote a joint letter to the Washington, D.C. Department of Consumer and Regulatory Affairs regarding the District's well-publicized Green Building Act of 2006, which will eventually apply to all public and private construction in D.C. over 50,000 square feet and require either a Certified or Silver LEED rating, depending on the type of project.

In a recent newsletter describing the scope of the letter, Mark H. McCallum, general counsel to NASBP, noted that "[i]t is evident from a reading of the 'performance' bond requirements contained in the new law that the underwriting and operation of surety bonds was not well understood by the drafters." Mr. McCallum's letter to the Department of Consumer Affairs, authored in cooperation with Matthew Klimczak, Director of Underwriting for SFAA, both points out numerous, significant concerns implicated by the D.C. legislation for the surety industry, as well as suggests broader implications for green building legislation at large that local governments should remain vigilant of when considering such mandates in both the public and private sectors.

McCallum and Klimczak first point out that D.C. Green Building Act incorrectly uses the term "performance bond." A performance bond is generally issued by a surety and assures one party (for example, the owner) that another party (such as its general contractor) will perform as required under its contract. In the event that the latter party doesn't perform, the surety will step in and determine what steps are necessary to make sure that both the contract is completed and the project itself is finished. However, the D.C. Act's concept of a "performance bond" in Section 6 is ostensibly designed to serve as a penal sum in the event that a project does not meet the requirements of the Act, to be deposited into a Green Building Fund and used to fund staffing, inspections, and green building education programs.

Moreover, there is no language in the Act that designates which party on the project must supply the "performance bond." McCallum and Klimczak note that the LEED program, necessarily, involves a large number of project stakeholders- from designers to contractors and suppliers- who "all may have responsibilities that bear upon the fulfillment of the LEED criteria." Although the owner is in the best position to make sure that the LEED requirements are met, the Act does not expressly prohibit- or permit- the delegation of the bond requirement from the owner to any of those types of parties. If such an owner did delegate its bond-procuring duty, a surety would likely decline to issue the bond because "neither the design professional's nor the contractor's responsibilities will involve the complete [project] undertaking," making the surety leery of such a party's ability to physically control the project's completion.

McCallum and Klimczak next identify an "inherent conflict of interest" in the Act. The staff

responsible for evaluating compliance are those whose positions are being funded by projects that forfeit the "performance bond" into the Green Building Fund. As the authors accurately point out, "[t]his will impose considerable tension on objective verification of green building requirements." The letter concludes by observing that many other bond-related considerations are not addressed by the Act as drafted, and requests a meeting with the Department of Consumer Affairs after noting that "[w]ithout needed clarifications and modifications, sureties likely will be reticent to write these 'performance bonds.'" It's not clear whether this meeting has taken place yet, or what type of response the letter has solicited from the D.C. government, but we'll obviously be keeping track of the surety industry's position with respect to the D.C. legislation.

From a broader point of view, green initiatives are rapidly changing the scope of responsibility that owners are requiring from construction project stakeholders. All parties- legislators, owners, contractors, and design professionals- must be aware that their risk profile can- and in many cases has- changed, and guide themselves accordingly in order to achieve the desired sustainable outcome.

Don't Let Green Design Cause Red Ink ,
by Frank Musica, presentation to the American Institute of Architects
The types of exposures on sustainable projects are not different from those on other projects but the prudence is necessary to avoid losses:
•Interest in green design often generates unreasonable expectations or onerous contractual obligations such as guarantees.
•Any green design project should be approached with greater communication, comprehensive documentation and a clear and mutual understanding of scope, goals and limitations.
•Increased services and value should result in increased compensation.

(Cases)

- Architect agrees to design to acquire enough points for Gold certification. Developer advertises planned office building using superlatives about "reduced operating costs and healthier and more productive occupants" from USGBC information to attract tenants at higher rents. Budget and time constraints prevent certification as Gold. Developer sues for negligence, breach of contract and breach of warranty based on architect's "guarantee" of Gold certification.
- Architect, landscape architect and client agree on extensive green roof installation. Water infiltration causes significant direct and consequential damages. After analysis it is determined that cause is inadequate structural stability. Structural engineer claims that proper information on roof use and installation was not provided. Architect had limited structural engineer's liability to $50,000.
- University agreed to architect's design of operable sash for library despite concerns over effect of untreated air on building's operations. Architect stress importance of outside air for health and alertness of students. Solar shading for energy conservation provides shelter for pigeons. Students report respiratory illnesses when using library. Newspapers report "epidemic." Parents express concern. Architect sued for negligence because of introduction of diseases contained in pigeon droppings.
- Insurance company wants green products in redesign of interior space. Design firm specifies cork flooring in kitchen areas. Damage to cork flooring in high-traffic areas by sinks, ice machines and coffee makers results in water retention and growth of mold. Employees not satisfied with attempts to clean and seal floors with environmentally safe solutions. Cork

tiles are replaced with vinyl flooring.

- Design team develops efficient process for moving solar shading for building. After project is completed, owner gains publicity because of innovation. Owner also attracts attention of company that has valid patent on similar system. Patent holder demands significant licensing fee or the removal and destruction of the solar shading system. Owner sues architect as prime professional based on negligence in not researching patent and to enforce contractual provision that requires architect to defend and indemnify client for any intellectual property infringement.
- Client is government contractor providing military systems designs and terrorism identification services. Client invests in green design that includes extensive daylighting systems. Federal government determines that government contractor is putting confidential information at risk because of windows and skylights and threatens to revoke government contractor's security rating, cancel existing contracts and prevent future consideration. Client sues architect citing that standard of care was breached because architect was aware of client and government security concerns.
- Architect made decision to use green product from new manufacturer whose promotional information was impressive. Architect shared promotional information with owner who, based on architect's opinion, agreed to its use. Product was not readily available. Project completion was delays and construction schedule distorted. Contractor demanded increased payments for overhead, lost profits and out-of-sequence construction. Owner brought claim against architect since architect never informed owner that product was subject to delayed delivery.
- Project owner agrees to design that uses domestic stone. Contractor approaches owner with option of using stone quarried in India, finished in Italy and installed in Vermont for cost savings. Architect "discovers" substitution, argues with owner about violation of green design because of high embodied energy in imported stone. Architect releases information to press about substitution. Architect sued by owner for violation of confidentiality agreement and by contractor for defamation.
- Lured by the promise of "healthier and more productive occupants" basic to LEED® publicity, tenant rents space in Silver certified building. At end of first year, tenant's records indicated greater use of sick leave, increased complaints by employees about eye strain and drafts, and reduced output by clerical staff. Tenant demands rent rebate from project owner based on promise of a healthful workplace and tenant sues architect.
- Architect designs facility to meet existing codes and standards including local laws concerning sustainability. Public pressure produces political action that changes requirements as project is in construction. Owner is forced to delay project for redesign to meet new requirements and changed interpretations. Architects wants to be paid for redesign. Owner sues architect stating that a reasonable architect would have been aware of impending changes and therefore is responsible for redesign, reconstruction and delay damages.
- Construction company signs design-build contract for green design. Design-builder "educates" owner that many problems with sustainable design can occur based on incompetence of design professionals. Owner agrees with design-builder that it will pursue remedies directly against design team if problem occurs. Design-builder assigns rights to sue subcontracted design team members and agrees to assist owner in any litigation. Design-builder signs design subcontracts with design team. Problems occur (delays, extras, constructability issues, mold) and owner sues design team firms directly.
- County government requires recycling of construction materials existing on site and excess to construction. Architect designs green project that requires recycling. Architect agrees to

construction observation services. During construction, contractor determines that prices for recycled steel and other materials have declined, project is delayed by recycling obligations, and lower tipping fees in another state would save time and money. County finds out about dumping and takes legal action against project owner. Owner sues architect based on architect's duty to observe construction services and failure to identify and prevent dumping.

- Green design includes use of sealants that are "environmentally friendly" to achieve sustainability designation for client that is a national environmental association. Subcontractor uses wrong sealant claiming that sealant was improperly specified and even if properly specified would not have worked. Sealant has to be removed; subcontractor declares bankruptcy. Both indoor air quality and association reputation degraded by use of wrong sealant. Claim against architect includes improper specification and negligent construction observation.
- Architect designs building recognized for innovative sustainability attributes. Project owner agrees to allow photography of exterior and interior to be used by architect in articles and promotional material. Architect enters award competition and provides details of floor plans, mechanical systems and building structure without further approval by owner. Owner seeks injunction against public display and damages because of violation of confidentiality and security interests.
- ConsultantProject owner recommends LEED®Accredited Professional to architect. Architect agrees to hire person as consultant to assist on sustainable design. Consultant recommends specific materials and systems. After construction owner is dissatisfied because of increased up-front cost, questionable quality, construction delays, and energy costs that are higher than anticipated. Owner sues architect; architect blames advice of consultant. Consultant has no professional liability insurance coverage or attachable assets.
- Homeowner is interested in architect designing a low-cost addition that would provide a healthful interior and save on energy costs. Architect agrees to design a "state-of-the-art" green residence for homeowner. Discusses expertise and how design and service will "assure" client of satisfaction with an on-time and within-budget project. Owner is unhappy with cost, time and result. Sues architect under consumer protection laws, alleges fraud in the inducement to the contract for services, and demands rescission of contract and return of fee even though design and construction are complete.
- Firm uses Building Information Modeling system for energy analysis and constructability. Client appreciates ability of firm to respond quickly to requested changes during the design process. Based on client's continually increasing awareness of the latest in sustainable design, client constantly requires changes in design and analyses. Firm accommodates client demands even though its contract does not specifically allow it to modify its compensation to meet the increase in services. Firm attempts to collect additional fee; client sues for negligence stating that changes were the result of the firm's failure to understand sustainable design requirement.
- Design team agrees to three-school project that would serve as examples of sustainable design and energy conservation. Using appropriate design standards and including commissioning efforts, schools are completed and put into service. Architects and consulting engineers signed contract that stated that projects would "reduce operating costs by 50 percent" over schools of similar size. Energy usage is comparable to other schools recently designed and constructed. School system is publicly embarrassed, disappointed and blamed as being "hoodwinked" by architect and engineers. School system brings claim.
- Architect agrees to design to owner's specific construction budget. Construction costs escalate and specialty contractors knowledgeable in sustainable construction cost more than

projected. Bids come in over budget. Redesign reduces scope and quality. Rebids come in over budget because of further cost escalation. Additional redesign significantly delays schedule and still is over budget. Owner did not agree to limit architect's liability to redesign. Architect sued for increased financing costs, lost opportunity costs and other expenses.

- Law firm noted for its lobbying expertise hires architect to design new offices at a level of green design that would attract positive attention. Architect obtains promotional information from manufacturers of products and systems and based on promotional information provides plans and specifications to attention-getting green design. Local press looks into materials and systems used and claims that sustainability is not as promoted. Firm is held up to ridicule beyond that attributed to its lobbying. Firm denies attempt to "greenwash" project and publicly blames architect through demand for remediation and apology.