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CLAIMS

Insurers Worry About Green-Building Risks

Sustainability-market euphoria masks subtle liability issues unique to green building

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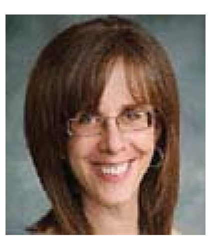
By Gary J. Tulacz

It seemed to be a straightforward task: An owner needed a new facility and wanted it to be sustainable and employee-friendly. The architect provided a design that included extensive daylighting systems to provide more natural light. The problem? The owner was a defense contractor, and the federal government determined that large windows and skylights posed a security risk. It threatened to revoke the owner's security rating, cancel existing contracts and bar future contracts. The owner sued the architect.

"It was a typical case where a government contractor had outgrown its old facility and wanted a new, employee-friendly building," says Frank Musica, senior risk management attorney for Victor O. Schinnerer & Co., a Chevy Chase, Md.-based underwriting manager for insurance giant CNA's professional liability program. Musica, who has assembled a large collection of claims related to green building (see p. 11), notes that this claim "went away" after the owner was able to sell the building at a premium price. "There has not been a major court ruling on a green-building risk yet, but there will be," he says. And the insurance industry is concerned about risks associated with building green, sources say.



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The scope of the risks and concerns over building green can be seen in a new insurance study by Marsh, a New York City-based broker and risk manager. The emerging risks of claims include failure to obtain the promised green certification for a project, failure of a green design to deliver expected results, problems with new products and designs, and delays from lack of green-product availability, the study found.

The study also discovered that there are no new insurance products to address risks specific to the green market. "In the general-liability arena, underwriters are terrified," says Catha Pavloff, head of Marsh's Green Team and author of the report. She says underwriters have yet to gauge the risks unique to green building and do not know how to position or price products covering liability in that market.

"The number and scope of the risks have not been sorted out yet, and they probably won't be for another 10 to 15 years," says Stephen Bushnell, a director at Novato, Calif.-based insurance giant Firemen's Fund. In October 2006, it introduced a Green-Gard suite of property-insurance products to cover green buildings certified under the U.S. Green Building Council's Leadership in Energy and Environmental Design program, but it does not have a green-building liability product. "I don't think any of our competitors have introduced liability products yet, either," Bushnell says.

The risks of building green only now are being assessed seriously. "In the early stages of the green movement, it was OK not to grapple with risk issues because there wasn't that much at stake," says Edward B. Gentilcore, partner in Duane Morris LLP, a Pittsburgh-based law firm. But now, failure to achieve LEED certification or comply with local sustainability laws may place such things as tax incentives, occupancy allowances and premium-rate leases at risk, he says.

No Guarantees

A major area of risk is in obtaining certification under LEED or other similar programs. Pavloff says a designer's standard of care in seeking LEED certification should be spelled out in the contract, and that changes in that standard should be measured against what a prudent designer would have done. But "designers should never guarantee LEED certification," she says.

New products are another area of concern. "What happens if a system or product fails or doesn't live up to its promise?" asks Musica. He says this is very significant given recent high energy costs, when energy efficiency often is a key selling point for a green building. "If a product fails and the manufacturer's warranty has expired, the owner will likely go after the designer," Musica says.

Letting green building get bogged down in claims will make it more expensive and less attractive.

— EDWARD B. GENTILCORE, PARTNER, DUANE MORRIS LLP

Products and processes are not the only concern; there also is a question of risk allocation. No party controls all of the elements needed to achieve LEED certification, so there will be a struggle over defining who bears the risk. Gentilcore says it is especially critical in building green for parties to determine what they can control and spell out the risks and responsibilities in the contract.

A Sampling of "Green" Claims Against Architects

- **Guarantee.** Architect agrees to design for LEED Gold certification, then the developer sells leases on this basis. Budget and time constraints prevent certification as Gold. Developer sues for negligence, breach of contract based on architect's "guarantee."

- **Green Roof.** Water infiltration on green roof causes damages because of inadequate structural stability. Architect sued.

- **Mold.** Design firm specifies cork flooring in kitchen areas. Floors in high-traffic areas by sinks, ice machines and coffeemakers result in water retention and mold.

- **Greenwashing.** Architect specifies green design based on manufacturers' literature. Newspaper claims sustainability is not as promoted, embarrassing owner. Owner denies "greenwash" and blames architect.

- **Unintended Consequences.** Architect designs operable sash for university library, stressing importance of fresh air. Solar shading provides shelter for pigeons. Students report

Many contractors have developed policies requiring contracts to be clear on the firm's responsibilities for earning LEED points and have called for procedures to be put in place on each job to ensure LEED compliance. This includes requiring documentation up front, rather than chasing it after the job is done.

Unexpected delays caused by LEED processes are another worry among contractors. Processes like flushing the air in a new building is a "time hog," says one, which could present problems where there is a hard finish date and liquidated damages for late completion. Further, delays caused by a lack of availability of green products due to hot demand could result in increased costs. Gentilcore urges firms to strengthen force majeure clauses in their contracts to protect themselves against unexpected delays.

There are further complications in that more state and local jurisdictions are encouraging or requiring specific levels of sustainable design and construction. There are nearly 70 jurisdictions in 28 states that call for some form of green

respiratory illnesses when using library. Architect is sued for negligence for introducing diseases contained in pigeon droppings.
Source: Frank Musica, Victor O. Schinnerer & Co.

building. Many legal experts believe that if a building falls short of these requirements, the designer and contractor could be subjected to negligence claims.

Insurers and many industry firms say good management and risk practices should protect contractors and designers. "Right now, the risks in green building should be handled through existing risk-management techniques," says Musica. Pavloff notes that Marsh's Green Team is holding sessions around the country to alert all members of the construction process—designers, contractors, suppliers and owners—of the risks and how to manage them.

For many in the industry, resolving the risk issue is critical for green building to succeed. "We need to get these questions addressed because sustainable design is an important issue for the nation and the environment," says Gentilcore. "To let the process get bogged down in claims will only make green building more expensive and less attractive, and that doesn't help anyone."