

What's Your Green Construction Strategy?

By Chris Cheatham, LEED AP¹

“Businesses that ignore the debate over climate change do so at their own peril,” warn the authors of the book Climate Change: What's Your Business Strategy. The authors suggest that businesses should think of climate change as a burgeoning market opportunity instead of an environmental burden and that forward-thinking parties will be rewarded for acting early. In this regard, one of the fastest growing markets spurred by the debate over climate change is green construction.

One factor contributing to the boom in green construction is an increase in cities, states and regions enacting green construction laws. For example, green construction projects have been undertaken in Washington, D.C. thanks, in part, to the Green Building Act of 2006. As governments rush to enact green construction laws, parties will face new responsibilities and potential liabilities while the market will demand new practices, products and tools to comply. This article will focus on new responsibilities created by the performance bond requirement in the Green Building Act of 2006 and the market's reaction to this new requirement. This scenario will illustrate the new risks created by green construction regulations and the need for parties to develop strategies now to manage those risks.

Green Construction

The aim of green construction is to incorporate design and construction practices that decrease a building's use of energy, water, and materials and that reduce a building's impacts on health and the environment through better siting, design, construction operation and maintenance. Green construction provides three primary benefits: (1) lower operating costs; (2) improved public and occupant health; and (3) reduced impacts on the environment.

The preeminent system for measuring a building's "greenness" is the Leadership in Energy and Environmental Design ("LEED") rating system created by the U.S. Green Building Council ("USGBC"). Under the LEED rating system, buildings are scored based on five major categories: (a) sustainable sites; (b) water efficiency; (c) energy and atmosphere; (d) materials and resources; and (e) indoor environmental quality. Different LEED scoring systems apply to different types of projects and increased green performance results in higher ratings: certified, silver, gold or platinum. The USGBC determines certification after an applicant submits documentation showing compliance with the requirements of the applicable rating system.

In recent years there has been an increased interest in green construction due, in part, to the recognition of economic benefits associated with this type of construction. These

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economic benefits are the result of savings in the use of energy and water and increases in profits and asset values. For example, a study released in March 2008 by CoStar Group concluded that that “sustainable ‘green’ buildings outperform their peer non-green assets in key areas such as occupancy, sale price and rental rates, sometimes by wide margins.” Government regulations and incentives have also spurred green construction. In 2006, Washington, D.C. became the first major U.S. city to require LEED compliance for both public and private projects.

The District’s Green Building Act

On March 8, 2007, Washington, D.C. passed the Green Building Act of 2006 (“Green Building Act”), which phases in green building requirements for different types of buildings over the next five years. The Green Building Act contains both LEED and non-LEED requirements for projects depending on the size, classification and schedule of the project. This article will only focus on the LEED and performance bond requirements. Contractors, designers, owners, sureties and other parties affected by the Green Building Act should consult a LEED Accredited Professional and a construction attorney to learn more about the Act’s complexities.

The Green Building Act differentiates between two types of buildings – publicly- and privately-owned buildings – in determining deadlines for the compliance with green building requirements. Starting March 8, 2007, new construction or substantial improvements (hereinafter, “new construction”) of publicly-owned, nonresidential buildings must fulfill or exceed LEED Silver standards. New construction of publicly-owned residential buildings greater than 10,000 square feet must satisfy the Green Communities 2006 standard. Finally, tenant renovations to at least 30,000 square feet of a publicly-owned building used for commercial purposes must comply with the LEED certification level.

Requirements for privately-owned buildings will be phased in over the next several years starting on January 1, 2009. On that date, parties submitting building construction permit applications for privately-owned buildings must also submit a USGBC green building checklist. The USGBC’s green building checklist is used to calculate a building’s estimated LEED score as the project progresses. After January 1, 2010, nonresidential, privately-owned projects submitting the first building construction permit for new construction of 50,000 square feet or greater of real property acquired from the Government of D.C. must comply with the LEED certified standard. Finally, after January 1, 2012, all new construction of projects 50,000 square feet or greater must comply to the LEED certification level. The Green Building Act also provides incentives for entities participating in green construction in the form of grants and expedited review of construction documents.

One of the most controversial provisions of the Green Building Act is the performance bond requirement. Like the LEED requirements, implementation of the performance bond requirement depends on the date when specific construction events occur. Prior to January 1, 2012, “commercial applicants” who apply for incentives under the Green

Building Act must provide a performance bond, which is due and payable upon approval of the first building construction permit application. After January 1, 2012, an applicant for construction of a privately-owned building must provide a performance bond which is due and payable prior to receipt of a certificate of occupancy. Thus, after January 1, 2012, if a construction project must meet green requirements in the Green Buildings Act, the “applicant for construction” must also provide a performance bond guaranteeing satisfaction of the green requirements.

Furthermore, the Green Building Act sets substantial amounts for the required performance bonds. If the performance bond is required prior to January 1, 2012, the bond must equal 1 percent of the incentives received. If the bond is required after January 1, 2012, the bond amount increases based on the project size from two to four percent of total cost of the building, but is not to exceed \$3 million. Most importantly, if the building fails to meet the “verification requirements” in the Green Building Act, “the performance bond shall be forfeited to the District.” For example, a 72,500 square feet privately-owned building with a total cost of \$28,000,000 being constructed after January 1, 2010 that fails to meet the appropriate LEED certification level would forfeit a performance bond in the amount of \$560,000 to the D.C. government.

The Insurance Industry’s Response

In an August 13, 2007 letter, the Surety and Fidelity Association of America (“SFAA”) and the National Association of Surety Bond Producers (“NASBP”) responded to the Green Building Act’s performance bond requirement, stating that the Act “includes bond requirements that, if not clarified significantly, may make sureties reticent to issue such bonds.” The SFAA and NASBP outlined several problems with the Green Building Act’s performance bond requirement, including:

- The Act incorrectly uses the term “performance bond” as the bond described in the Act “seems to function more in the manner of a license or compliance bond, which typically guarantees compliance with a law or code.” A performance bond typically assures one party that another party will perform the contract in accordance with its terms and conditions.
- The Act does not designate which party is to furnish the performance bond. The letter argues that “the building owner or developer, as the originator of the building project that retains the design professional and contractor, hold the ultimate responsibility for whether the building achieves compliance with the Act’s requirements.”

The SFAA and NASBP’s primary concern with the Act is that contractors and performance bonds are improperly suited for guaranteeing compliance. As more owners and governments demand green construction, the party and mechanism for ensuring “green” compliance must be carefully articulated. The only party with control over a project from start to finish is the owner or developer. Designers control a majority of the

green features that are incorporated in a project, but they cannot ensure these features are constructed properly. Contractors can guarantee that a building will be built according to the “green” plans and specifications, but contractors are reluctant to accept responsibility for design errors and omissions. Contracts must be examined closely to determine who is responsible for green construction compliance.

Washington’s Green Building Act and the insurance industry’s reaction represent a powerful case study of the future of green building regulations. In response to growing concerns about global warming and buildings’ environmental impacts, more and more cities will enact legislation that quickly sweeps in green construction requirements. Parties can anticipate these new regulations now by creating innovative green construction practices, products and services. Those parties will not only ease their compliance with future regulations, but they will gain credibility and position themselves to influence the policy-making process before regulations are adopted. Others will do nothing now and be forced to adapt to whatever green construction regulations eventually take effect. What will your strategy be?