

## Seeking a Safe Harbor: Can ASTM's BEPA Help Sellers Avoid Liability?

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How do you know if a certain commercial property is energy efficient or inefficient? If the building is LEED-certified, what exactly does that mean with regard to the building's energy use and costs? These days, potential buyers (and the lenders behind them) seek to understand the relative energy efficiency of a building beyond the fact that an EPA Energy Star plaque is hanging in the lobby. A meaningful energy evaluation tool - like ASTM's *Standard Practice for Building Energy Performance Assessment for a Building Involved in a Real Estate Transaction* (E 2797-11) ("BEPA") - is useful in analyzing the energy consumption of a building. However, as energy disclosure laws ripen into fruition across the country, and building purchase agreements increasingly address the energy concerns of buyers, ASTM's BEPA could serve as a safe harbor from potential liability in the context of commercial real estate transactions.

With the growing interest in green building and green certifications, it is easy to understand why property due diligence conducted by prospective buyers and lenders may include a focus on energy efficiency. While energy efficiency is not as flashy as solar panels or wind turbines, it is a very cost-effective energy conservation measure. Energy efficient buildings should increase property value and even command more attractive financing opportunities from lenders. But before the market can recognize (and reward) energy efficient buildings, it needs a standardized methodology to collect and analyze building energy-use information. For the first time in the industry, ASTM's BEPA satisfies this need for a consensus industry standard approach.

But what if the BEPA could do more than factoring energy efficiency into building valuation? What if the BEPA could be used to deflect accusations of false or misleading representations about a building's energy performance levels?

Consider the development of ASTM's E 1527 Phase I Environmental Site Assessment (ESA) Standard as a useful corollary. ASTM E 1527 was created to assist users in their efforts to qualify for the CERCLA landowner liability defenses. The main thrust of ASTM E 1527 was to standardize "all appropriate inquiry" so that users could qualify for safe harbor for future, potential discovery of contamination on their property. But complying with AAI had a secondary benefit - helping users make informed decisions regarding their real estate investment options. Phase I ESAs are very useful to prospective purchasers and investors in narrowing the field between otherwise comparable properties for sale.

ASTM's BEPA has nothing to do with CERCLA. It was generated in response to building energy performance labeling, benchmarking, and disclosure laws that require an owner to disclose the building's energy use at the time of sale, lease, or financing. These laws were drafted to encourage owners to improve their buildings' energy efficiency and reduce their carbon emissions. And understanding how each building is performing relative to its peers can dictate how a prospective purchaser (or lender) evaluates investment property options. However, the BEPA may too have a secondary purpose - to minimize the user's potential liability and risk, whether it be complying with state and local energy benchmarking and disclosure laws or responding to energy efficiency inquiries in a purchase agreement in a non-mandatory disclosure state or locale.

Sellers in the commercial real estate context may need protection. The current building benchmarking

and disclosure laws in effect today are relatively new and rapidly evolving. As recently as February 2011, San Francisco passed an energy ordinance requiring commercial building owners to disclose annual energy benchmarking and perform energy audits every five years. This law complements California's state law (AB 1103), which requires commercial building owners to disclose energy use information, such as the property's Energy Star Portfolio Manager rating and other data, to parties involved in the sale, lease, or financing at the time of the transaction. By way of a 2009 mandate, New York City requires auditing, retro-commissioning, and benchmarking. Seattle and Washington State are other examples of cities and states that have benchmarking regulations on the books.

As these laws gain traction in the marketplace, prospective buyers and lenders will begin relying on the data submitted to make investment decisions. And therein should lie the concern for sellers interested and willing to comply with disclosure regulations: what if the information being provided is incomplete or inaccurate?

Consider Senate Bill 5854, which became effective in Washington State in July 2009. Based on specific size guidelines, S.B. 5854 requires a building owner to disclose U.S. EPA's Energy Star Portfolio Manager benchmarking data and ratings to a prospective buyer, lessee, or lender for the most recent 12-month period. But S.B. 5854 also states that "nothing in this section . . . alters the duty of a seller, agent, or broker to disclose the existence of a *material fact* affecting the real property." If you are a seller in Washington State, what other "material facts" beyond the Energy Star benchmarking data and rating are required to be disclosed? What type of due diligence is necessary to uncover "material facts" connected to a property that could impact its energy performance? More importantly, what are the consequences for failing to disclose (or even recognize) such "material facts?"

Also consider the actual text of the new San Francisco ordinance discussed above, which states that owners of nonresidential buildings must "conduct Energy Efficiency Audits of their properties and file Annual Energy Benchmark Summaries for their buildings, and *mak[e] environmental findings*." Unclear is what additional "environmental findings" may need to be provided (above and beyond the energy audit and information required in the AEBS) to satisfy San Francisco's disclosure requirements. To the extent "environmental findings" associated with commercial property are withheld from the prospective purchaser, which down the road negatively impacts its energy performance, could the former seller be liable for the property's potential devaluation in the market years after the sale? A clever attorney may figure out a way to convince a fact-finder to say "yes."

To use the San Francisco ordinance again as an example, it requires the owner of a non-residential building to disclose the energy use intensity per unit area per year (kBtu per sq. ft. per yr.) for a building. But how do you factor in building operating hours or building vacancy? How do you take into account a major building renovation that occurred two years prior to the energy use analysis? The San Francisco ordinance also requires disclosure of the weather-normalized energy use intensity per unit area per year (kBtu per sq. ft. per yr.) for the building. But how exactly should weather conditions be factored in?

The ASTM BEPA standard was developed to "fill-in the blanks" when measuring the energy performance of a building in response to regulations in Washington State, San Francisco, and elsewhere. However, as more of these regulations are integrated into the marketplace in the coming years, and commercial real estate transactions are made (and some inevitably regretted) as a result thereof, the BEPA could function as a safe harbor protection for sellers. Until there is consistency within state and local regulations in terms of what building energy-use information is required to be disclosed and/or benchmarked, the BEPA could serve the industry as a guide to the degree of due diligence required to satisfy such laws.

To be fair, the majority of states do not have mandatory building energy performance disclosure requirements. Nonetheless, the terms of a lease or purchase agreement will always dictate the priorities of the transaction. Even if there is no law mandating disclosure, a lease can still address energy concerns, and a real estate purchase agreement can require a building to sustain specified energy performance levels. Under these and similar circumstances, what will sellers be held accountable for? Is it sufficient to simply report that your building has an Energy Star rating of 75? Will buyers or lenders be satisfied with simply receiving a number to indicate the energy performance of the property in connection

with a sale? This author doesn't think so.

As parties to commercial real estate transactions become more sophisticated in terms of assigning value to energy efficiency, it is reasonable to expect prospective buyers to insert specific energy performance warranties into their proposed purchase agreements. In doing so, sellers may be asked to disclose information about the building's energy usage beyond the Energy Star rating alone. Buyers today may want information about the building's fuel supply, availability of tax incentives and government grants, or renewable energy options. If buyers pose these questions in their purchase agreements, sellers will need to answer them.

Over time, as sellers begin negotiating and responding to building energy performance criteria in the commercial real estate context, the ASTM BEPA may be a useful methodology in terms of demonstrating their willingness and ability to satisfy that criteria. The ASTM BEPA could also offer protection to the seller from disappointed, litigious buyers who are of the opinion that the building is not measuring up to energy efficiency representations made in a purchase agreement.

In sum, the ASTM BEPA standard was designed as a voluntary building energy performance assessment methodology. But it could function as a safe harbor under mandatory energy consumption disclosure laws from potential liability for future discovery of building energy use misinformation that negatively impacts value. Even in those states where such energy disclosure laws are not yet on the books, the ASTM BEPA could diffuse allegations of misrepresentation and breach of express/implied warranties in the context of a commercial transaction while at the same time, for the reasons explained above, enhance the value and marketability of the property. As such, sellers and agents should strongly consider seeking the input of counsel and consultants knowledgeable about the BEPA in the context of any commercial real estate sale or purchase.