Liability Aspects of Home Energy Rating Systems

P. L. Hendrickson

October 1983

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PREFACE

This report is the fourth in a series of reports on the subject of home energy rating systems. These systems are designed to provide information on the relative energy efficiency of residential housing to housing consumers and professional people involved with residential housing. The principal focus of this report is on possible liability issues associated with implementation of a rating system. An introduction to the rating system concept is also included.

The three previous reports in this series are:

1. P. L. Hendrickson, B.A. Garrett-Price, T.A. Williams, Pacific Northwest Laboratory, Overview of Existing Residential Energy-Efficiency Rating Systems and Measuring Tools, PNL-4359, October 1982.
2. M. L. Frankel, J. A. Duberg, Centaur Associates, Inc., Washington D.C., An Evaluation of the Home Energy Rating Concept and the Massachusetts Pilot Project, PNL-4764, June 1983.
3. A. Ackerman, M. K. Cox, E. Tarini, Energyworks, Inc. Watertown, Massachusetts, and L. Schuck, Alliance to Save Energy, Washington, D.C., The Massachusetts Home Energy Rating Project, PNL-4763, August 1983.

Preparation and publication of these reports has been supported by the Office of Building Energy Research and Development, U.S. Department of Energy, John Millhone, Director. Susan Heard of the Office has provided guidance for the work and served as the DOE technical monitor and project officer for all four reports.

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SUMMARY

The principal topic of this report is liability aspects of home energy rating systems. An introduction to the rating system concept, including types of rating systems, implementation efforts to date, and possible groups to conduct ratings, is also included. The home energy rating system concept involves the periodic rating of the energy efficiency of residential buildings. The rating can provide a relative indication of a home's energy efficiency and also a quantitative estimate of consumption, fuel cost, or both.

The U.S. Department of Energy is interested in home energy ratings as a means of promoting residential energy conservation in a non-regulatory fashion by providing energy-efficiency information to housing consumers. Conservation can potentially occur in several ways, all of which relate to the fact that ratings facilitate the incorporation of energy-efficiency considerations into market value. The construction of energy-efficient homes and the retrofit of existing homes with features to improve energy efficiency is likely to be encouraged because a rating should give builders and owners more confidence that their incremental energy conservation investment can be recaptured at the time of sale. A rating will also facilitate comparison shopping by home buyers and tenants. Sellers and landlords in high vacancy or high energy cost markets may feel they need to improve energy efficiency to attract energy-conscious buyers and tenants. There is also the potential for social pressure on owners to obtain a high rating. Finally, a rating can facilitate the purchase of an energy-efficient home by a buyer who only marginally qualifies for a loan; the expectation of lower energy costs permitting greater debt repayment capacity enables a lender to lend more money than usual.

Actors associated with rating systems that have potential liability include the developer, the sponsor, and the individual rater. Once a rating has been performed, a homeowner or real estate broker/agent may incur liability if the rating information is misrepresented or not disclosed to a prospective home buyer or tenant.

The possibility of liability is a legitimate concern, but it should not be allowed to stop an otherwise desirable rating system or diminish the amount and

quality of rating information conveyed to housing consumers and real estate professionals. Liability has not been a significant problem in rating systems that have been implemented to date. No reported court cases involving energy rating labels were discovered during preparation of this report. Moreover, the economics of litigation do not favor liability claims. In most cases, alleged damages will be too small to justify hiring an attorney. Additionally, in the United States, unless modified by statute, successful plaintiffs are not able to recover their attorney's fees.

If a claim is made, there are several possible liability theories. The most likely claim against a developer, sponsor, or individual rater would be that a rating is faulty because of alleged negligence. Claims against a homeowner or real estate agent for misuse of rating information could be based on tort theories of misrepresentation or concealment of a rating, or a contract theory based on fraud or misrepresentation. There is also the possibility that disclosure of incorrect rating information or even nondisclosure of existing information can lead to liability under a state consumer protection statute.

There are a number of steps that can be taken by rating system participants to minimize the possibility of future liability. The most obvious step is to perform the rating tasks and disclose rating information in a diligent and careful manner. Another important step for the developer is to disclose to the rating system sponsor all assumptions and limitations associated with the rating system model. Similarly, the rating information provided the individual homeowner should clearly state the additional variables beyond the home's rating, such as family characteristics and energy consumption lifestyle, that can influence ultimate energy consumption, and can also include the key assumptions upon which the rating is based. Finally, complaint procedures for homeowners dissatisfied with their home's rating can be established.

In some cases, energy ratings will be sponsored and performed by employees of a governmental entity. Traditionally, governmental entities have not been liable for negligence in this type of activity. There is a trend in the law, however, away from immunity and toward treating the governmental entity as a private person. There are recent cases, for example, that hold governmental entities liable for negligent building inspections.

Disclosure of rating information can potentially impact the rights of a homeowner to privacy and to have such information kept confidential. Disclosure of the information to prospective home buyers and tenants is important though for a rating system to best achieve its goals of assisting the incorporation of energy efficiency into market value and encouraging energy conservation. As long as adverse rating information is not publicly advertised and the homeowner is notified ahead of time that disclosure to selected housing consumers and real estate professionals may occur, the possibility of violating privacy and confidentiality rights seems small.

1.0 INTRODUCTION

Home energy rating systems (HERS) are receiving increasing attention throughout the country. The concept involves the periodic rating and labeling of the energy efficiency of residential dwelling units. A HERS is analogous to the annual summary of fuel economy for new automobiles prepared by the U.S. Environmental Protection Agency. Residential energy-efficiency information would be available for use by home sellers/buyers, landlords/tenants, primary and secondary lending institutions, builders, real estate brokers/agents, real estate appraisers and tax assessors, and other user groups. In most cases the rating would be voluntary, and there would be no mandatory levels of energy efficiency that would have to be met. The rating can be structured to provide a home's relative energy efficiency in relation to other homes in the same climatic region and can also include an estimate of energy consumption, cost, or both. Candidate groups to conduct ratings include utilities, building inspectors, builders, real estate agents, and real estate appraisers.

The voluntary nature of a HERS is an especially important attribute in today's political climate where government imposed mandatory inspections and requirements are sometimes viewed with skepticism. It is possible that banks could eventually require a rating as part of an appraisal. However, by its nature a rating will have no mandatory elements associated with it. Home designers, builders, buyers, and renters will still be able to select the level of energy efficiency they desire, subject to applicable building codes.

This report focuses on potential liability issues associated with implementation of a HERS. Primary attention is given to liability issues associated with developing and performing ratings. Secondary attention is given to possible liability associated with misuse of a rating once it has been performed. Liability issues are important because organizations involved in performing and sponsoring ratings will naturally be concerned about limiting potential liability. It is desirable that the importance of liability issues be understood and put in perspective so that unfounded concerns are not permitted to defeat an otherwise beneficial rating system or diminish the quantity and quality of information provided the consumer.

Section 2.0 provides a background to residential energy efficiency rating systems by discussing likely beneficiaries of a HERS, types of rating systems, HERS implementation efforts to date, and likely rating groups. The discussion of potential liability begins in Section 3.0 with a brief discussion of why liability issues are important. Section 4.0 discusses who is potentially liable for misuse of ratings. General principles of liability and their application to particular HERS uses are discussed in Section 5.0. The duties of care that participants in an energy rating system owe to the public are discussed in Section 6.0. Subsequent sections discuss measures that may limit potential liability, possible defenses to liability claims, and privacy aspects of a HERS.

2.0 THE HOME ENERGY RATING SYSTEM CONCEPT

This section provides background information on the HERS concept. Included is information on likely HERS beneficiaries, types of HERS, implementation efforts to date, and likely rating groups. More detailed information on the HERS concept and implementation efforts is in a Pacific Northwest Laboratory (PNL) survey document,⁽¹⁾ two recent reports describing the results of a HERS field test in Massachusetts,⁽²⁾ the conference proceedings of a 1982 Summer Study on Energy-Efficient Buildings,⁽³⁾ and a report by the National Institute of Building Sciences.⁽⁴⁾ Some of the discussion in Sections 2.1-2.3 is adapted from a paper⁽⁵⁾ prepared by the author for the 1982 Summer Study.

2.1 HERS BENEFICIARIES

Implementation of a HERS is likely to benefit a number of groups. Perhaps the principal beneficiaries will be home sellers/buyers and landlords/tenants. An energy rating should help: 1) to facilitate price negotiation by providing both parties with relative energy-efficiency information and possibly an estimate of energy consumption and cost,⁽⁶⁾ 2) builders, sellers, and landlords to capture the market value of energy efficient improvements and thereby encourage the addition of such improvements, 3) the buyer/tenant to select among alternative home energy efficiencies and associated space conditioning costs. Home builders and real estate brokers/agents should benefit from the added information and assurance provided housing consumers by an energy-efficiency label. The construction and marketing of energy-efficient homes should be especially helped by ratings. To the extent a HERS operates to help achieve residential energy conservation, the nation's goals of saving energy are enhanced.

Real estate appraisers and tax assessors should also benefit from the information provided by a rating. If appraisers are asked to do an energy-efficiency rating, their workload will be somewhat increased; however, a thorough appraisal will ordinarily require a review of the energy conservation features of a home anyway. Consequently, the incremental time required for a rating may not be too significant. A rating/labeling system should also help

provide a systematic way for appraisers and tax assessors to evaluate a home's energy-efficiency features and facilitate comparison of home sale price information.

Primary and secondary residential lending institutions will benefit if additional information on expected utility costs are included in a rating or if the information can be readily obtained. This information can be used to assess the home buyer's ability to meet monthly payments and, hence, the maximum amount of money to loan. The buyer of an energy-efficient home will benefit if the lender is persuaded to lend more money than its usual underwriting guidelines indicate because of lower expected utility costs and, hence, increased ability to make loan payments.⁽⁷⁾ In some cases, a buyer will also be able to incorporate the cost of energy-efficiency improvements made at the time of purchase into his mortgage.

Finally, utilities and fuel suppliers should benefit by gaining knowledge of the relative energy efficiency of the housing stock in their service area. This information can be used to help assess the potential for reduced household energy consumption resulting from conservation programs and rising energy prices.

2.2 TYPES OF RATING SYSTEMS

Methodologies for assigning energy-efficiency ratings/labels to a residence can be conveniently grouped into three generic categories: prescriptive, calculational, and performance.⁽¹⁾ The particular advantages and disadvantages of each are discussed below.

2.2.1 Prescriptive Systems

The prescriptive category includes systems that assign points to various conservation features. The rating provided the homeowner is often a specific number of points. With most prescriptive systems, a given percentage change in points will not result in the same percentage change in expected energy consumption. Exceptions to this generalization include a system applicable to Minnesota prepared for the U.S. Department of Energy (DOE) by Lawrence Berkeley Laboratory (LBL)⁽⁸⁾ and a system prepared for the Tennessee Valley Authority

(TVA) by Total Environmental Action, Inc.⁽⁹⁾ Broader classifications such as descriptive terms (e.g. good or bad) and graduated categories (e.g., a "four star" home) have also been utilized.

Most rating systems that have been implemented have been prescriptive systems. The greatest number of implemented programs are investor-owned electric utility systems affiliated with Edison Electric Institute's National Energy Watch (EEI/NEW) program.

The system of point allocation for various conservation features is generally based on a heat load model or computational tool. Most often, the basis is the standard heat loss equations in the ASHRAE handbook.⁽¹⁰⁾ A few are based on computerized heat load models.⁽¹¹⁾ Others use a combination of models and trial and error to tailor a particular system to a specific climate.⁽¹²⁾ Often, the technical basis of a prescriptive system is not well documented, and it is quite difficult for a reviewer to assess the point allocation procedure.

The actual point score achieved by a home is not always communicated to the homeowner as part of the rating process. The reason for nondisclosure is perhaps related to concerns that the technical basis of a system does not justify a precise point score. A related consideration, discussed further in Section 7.0, is that possible liability for a negligently assigned rating is probably reduced with a broad classification. One important shortcoming of broad classifications is that the homeowner may not receive sufficient information to know the impact on his home's rating if specific conservation features are added. Without this information, there is likely to be reduced incentive to make conservation improvements.

2.2.2 Calculational Systems

This category includes calculational tools that can be used to estimate residential energy consumption. The estimate would then be transformed into a rating by indexing or by other methods. For example, a simple index/rating for a home could be its estimated consumption per sq. ft. divided by the average consumption per sq. ft. in the climatic region.

The number of tools in this category is large, on the order of 100-200, and they range from simple to complex. The simple calculation tools include

steady-state load calculations based on ASHRAE equations that can be performed on a four-function hand calculator. Simplified computer models include the LBL-CIRA model⁽¹³⁾ and the Energy Performance Design System developed by the Owens-Corning Fiberglas Corp. Homes that meet a designated minimum performance under the Owens-Corning System are designated "Thermal Crafted Homes." The recently completed HERS field test in Massachusetts utilized a calculational rating system with CIRA as a basis.⁽²⁾ Detailed public domain computer models include DOE 2.1, developed at LBL; BLAST, developed by the U.S. Army Construction Engineering Research Laboratory; and SUNCAT, developed by the National Center for Appropriate Technology. Generally, the more detailed the code, the more features are considered. Simplified codes many only consider building shell design load. More detailed codes can include heating, ventilating and air conditioning equipment; water heating; passive solar gains; and energy consumed by appliances.

Several reports that systematically review calculational methods are available.⁽¹⁴⁾ One caution in comparing the methods is that many procedures and associated computer codes are periodically updated. Consequently, the most current version should be obtained.

2.2.3 Performance Systems

Performance systems refer to ratings that are based on prior fuel consumption. A system might be implemented by gathering fuel consumption data for 1-2 years. The actual consumption would be compared to average consumption on a Btu/sq. ft. basis to produce a rating. The rating would ordinarily be normalized to account for heating and cooling degree-days during the observation period.

Performance systems have significant advantages and disadvantages. The main advantage is a relatively straightforward, objective procedure for computing the rating. Since the rating will be based on metered consumption data and measurable climatic data, there should be few disagreements about the computed rating. There are also important disadvantages to performance systems. First, the rating assigned is heavily dependent on the energy consumption lifestyle of the home occupants during the observation period. In the past, lifestyle has been shown to be even more important than energy conservation features in

explaining consumption.⁽¹⁵⁾ Consequently, a rating obtained by using the energy consumption pattern of one set of occupants may be a poor indication of performance for future occupants. A second disadvantage is that new and recently remodeled homes cannot be rated with a performance system.

2.3 CURRENT IMPLEMENTATION EFFORTS

A recent DOE-sponsored HERS pilot test has the best publicly available documentation of a rating program. In terms of numbers of ratings performed, the greatest experience with implementation of residential HERS has been with programs affiliated with the EEI/NEW programs. Several other programs have gained some experience, and others are now in the beginning stages. Additionally, several states and units of local government are now administering energy conservation standards for new buildings that can effectively yield an energy-efficiency rating. The standards can be complied with by accumulating sufficient points assigned to energy conservation features or by a showing that the estimated calculated energy consumption is within acceptable limits. The example programs described in this section suggest that residential HERS are being recognized as a useful energy conservation tool and are being implemented by utilities, various units of government, and even private groups.

2.3.1 DOE-Sponsored Massachusetts Field Test

A recent and well-documented HERS field test has recently been completed in Massachusetts.⁽²⁾ The pilot test was funded by the Office of Building Energy Research and Development, U.S. Department of Energy. Energyworks, Inc. of Watertown, Massachusetts, designed the rating system, with assistance from the Alliance to Save Energy, and served as project manager. The actual home energy-efficiency ratings were conducted by Mass-Save, a non-profit corporation formed by electric and natural gas utilities to conduct residential energy audits in Massachusetts. An independent evaluation of the field test was performed by Centaur Associates, Inc. of Washington, D.C.

2.3.2 EEI/NEW Program

The National Energy Watch (NEW) program is a loosely structured, voluntary, umbrella program developed for investor-owned utilities that are members

of the Edison Electric Institute (EEI). EEI provides a framework for assigning points to residential conservation features identified in the NEW Operating Manual.⁽¹⁶⁾ Homes that obtain 80% of the possible points for both thermal efficiency and the efficiency of electrical equipment and appliances, or that improve the point score of existing conservation features by 20% or more can be certified as NEW homes. Individual utilities can determine the conservation features to be included in their NEW program and the range of possible points to assign to each feature. The NEW program has been widely applied throughout the country. Approximately 170 utilities are using it in some form. It has been applied to single-family homes, condominiums, and mobile homes.

Users of a NEW certification need to be aware of several limitations. First, the technical basis of the point score is not likely to be available. EEI provides participating utilities with a nonmandatory sample point system for a climate with 3500-5500 degree days. There is no indication, however, of how points are assigned. Second, the point score will give an indication of how a home's conservation features compare to other homes, but no information on expected energy consumption or cost. Moreover, although the point score is likely to be monotonically related to energy consumption, it very likely will not be proportional. Third, the standard EEI/NEW program does not provide for special conservation features including passive and active solar. Some individual utilities have adapted the standard program to include special features.

2.3.3 Utility Programs Unaffiliated With EEI/NEW

The residential programs of Duke Power Co., Public Service Co. of Colorado and TVA provide good illustrations of utility HERS programs that are not affiliated with EEI/NEW.

Duke Power, with headquarters in Charlotte, North Carolina, certifies a residence as an Energy Efficient Structure (EES) if the home qualifies in one of two ways. The most common means of qualification is to meet specified conservation criteria that are based on the climate in the service area. The second means of qualifying is through a calculational procedure, conducted by the utility, that shows estimated energy consumption for the house less than or equal to estimated consumption of the house with all of the prescribed

conservation features. An unusual feature of the program is that EES-certified homes qualify for a lower power rate.

Public Service Co. of Colorado has developed the ECH₂OENERGY program in conjunction with the Denver Water Board and the Home Builders Association of Metropolitan Denver. A total point score or rating is computed for energy conservation and water conservation. The rating is done by builders, homeowners, or potential buyers. It is applicable to new and existing homes. The program has been available since January 1980, but is not currently receiving significant attention. This inattention is perhaps due to the lack of involvement of an institutional body in the rating process.

TVA has recently introduced its Energy Saver Home Program. The program includes both certification for homes meeting basic conservation features and a point system applicable to homes with more conservation features than required for a certificate. The point system is primarily oriented toward solar features, but does include points for conservation features that go beyond the minimum levels required for certification. The program is only applicable to new homes. Ratings are performed by builders.

2.3.4 Non-Utility Programs

The municipal program in Visalia, California, and the program in the Puget Sound area of Washington, coordinated by Western Resources Institute, illustrate residential HERS with no utility involvement. The City of Visalia initiated a residential HERS in January 1982. Points are awarded for energy conservation features and use of renewable resources. Homes are designated in zero- to four- star categories depending on how many points are obtained. Ratings are conducted by the city at no cost to the homeowner. Western Resources Institute is working with representatives of the appraising and lending community in the Puget Sound region to develop a HERS.⁽¹⁷⁾ The rating is designed to be performed by real estate appraisers acting for a lending institution when home ownership is transferred.

2.3.5 Building Codes

Several states now have building energy codes that can be met by accumulating sufficient points for conservation features or by a calculational

procedure showing that expected consumption is within designated limits. These codes can be easily adapted to a rating system for new buildings by simply indexing estimated consumption to produce a rating and by providing a mechanism to get the information to the home buyer/renter and other users of the rating.

Residential energy efficiency standards for new and remodeled buildings became effective in California in July 1982.⁽¹⁸⁾ The standards contain certain mandatory elements and also establish energy budgets for 16 climatic regions. The energy budgets can be met by a point system or a calculational procedure acceptable to the California Energy Commission. The State of Florida has building energy codes for both residential and commercial buildings.⁽¹⁹⁾ A point system is available as one means of compliance. Wisconsin has energy conservation standards applicable to new homes.⁽²⁰⁾ Building design heat loss calculations are performed by local building inspectors prior to issuance of a building permit. The resulting estimates could readily form the basis of a HERS. At the local level, the City of Boulder, Colorado, has an energy conservation point system applicable to new homes.

2.3.6 Northwest Power Planning Council

The Northwest Power Planning Council was created in 1981 by the Pacific Northwest Electric Power Planning and Conservation Act, P.L. 96-501. The Act required the Council to prepare a conservation and electric power plan for the Northwest region by April 1983. The plan issued by the Council directs the Bonneville Power Administration to provide technical and financial assistance to the housing industry for implementation of a uniform regionwide energy efficiency rating system for new and existing residential building. The system is to be fully implemented by January 1, 1986.⁽²¹⁾ BPA expects to complete its investigation of the use of ratings systems in the Northwest region by the end of 1984.⁽²²⁾

2.4 LIKELY RATING GROUPS

The key element in a successful HERS program is the delivery process. The greatest cost in implementing a HERS is the cost of the time for the individual who actually visits a home and makes the rating. The rating organization should: 1) be credible, 2) be willing to make ratings indefinitely into the

future, and 3) be able to make the rating at a low cost. Currently, most ratings are done by electric utility employees, largely because of the widespread use of EEI/NEW programs. Other possibilities include homebuilders in the case of new homes, building inspectors, real estate brokers and agents, real estate appraisers, and independent firms in the business of performing ratings. Utility personnel would likely assign a rating concurrently with performing an energy audit. Homebuilders could assign a rating any time prior to sale. Building inspectors could assign a rating at the final inspection of a new or remodeled home. Brokers could assign a rating at the time a residence is listed for sale. Appraisers would likely assign a rating when appraising a home for a lending institution that is considering lending money to a home buyer.

As long as the same rating methodology is used and consistency can be assured, there are likely to be advantages to having more than one group conduct ratings. More rating groups should increase the number of ratings performed and, thus, public awareness and usefulness of ratings. If it is assumed that any of the above groups would be willing and able to conduct ratings indefinitely, the principal criteria in evaluating rating groups are expertise/credibility and cost per rating. A third factor, usefulness, is applicable to the timing of the rating and is discussed below in conjunction with ratings by real estate appraisers. For the first two criteria, the possible rating entities can be ranked approximately as follows:

	<u>Expertise/Credibility</u>	<u>Cost Per Rating</u>
High	utilities, building inspectors independent rating firms appraisers, home builders	independent rating firms appraisers, brokers building inspectors utilities
Low	brokers	home builders

Based on this subjective ranking, utilities are the preferred choice because of high credibility and low cost. Utilities would be a preferred choice, however, only if the rating could be made in conjunction with an energy audit, and the future of residential energy audits is very much in doubt. If the auditor and

rater are the same person, credibility should be high because of the auditor's training and experience, and the incremental cost to conduct a rating over and above the cost for an audit should be low.

The National Energy Conservation Policy Act (NECPA) of 1978,⁽²³⁾ requires utilities with annual natural gas sales of 10 billion cubic feet or more, or 750 million kilowatt-hours of electricity or more to offer home energy audits to their customers on request.⁽²⁴⁾ The audits are to provide an estimate of installation cost and energy savings available from alternative energy conservation measures.⁽²⁵⁾ The utility is not required to provide the homeowner with an estimate of the total energy load or consumption for the home. The requirements are administered under the Residential Conservation Service (RCS) program within DOE. There are two important limitations to the future use of utility energy auditors to perform ratings. The most important limitation is that covered utilities are only required by Section 215(a) of NECPA to offer energy audits to their residential customers until January 1, 1985. Certain utilities may continue to offer audits beyond this date either voluntarily or because of provisions in state or local law. The second limitation is that under Section 210(9) of NECPA, energy audits are not available for new homes.

Building inspectors employed by local governments are credible candidate raters. They will generally only be available to rate new and remodeled homes. They could potentially function effectively in combination with utility personnel, since new homes are generally not audited for the reason noted above. In some communities, e.g. Davis, California, a building inspection is also conducted prior to a home sale. Inspections performed at the time a home is transferred may be done for a variety of reasons including inspecting for building code violations, illegal conversions of rooms to apartments, and required energy conservation retrofits. This type of inspection provides an excellent opportunity to also assign an energy rating.

Home builders are a candidate rating entity for new homes. Builders will naturally be familiar with the energy-efficiency features of homes they construct and they are in a good position to perform a rating at low cost. Some might argue that a builder performing a rating will result in an unacceptable conflict of interest. However, as discussed in Section 5, a builder is subject

to potential liability if a home is intentionally or negligently misrated. This consideration plus the builder's natural concern for his professional reputation should help to insure accurate ratings.

Real estate brokers/agents are another possible rating group. An advantage of brokers/agents is that they regularly inspect a house at the time of listing. Hence, the incremental cost to conduct a rating should be relatively low. Disadvantages are that the technical skills of brokers/agents to conduct a rating are likely to be appreciably lower than other potential rating groups.

Independent firms that specialize in providing energy ratings can undoubtedly become very skilled and efficient. Unfortunately the cost to produce a rating will be relatively high because the homeowner will normally be paying the full cost of the home visit and inspection. The estimated cost of an RCS energy audit in 1981 was \$150.⁽²⁶⁾ Preparation of an energy rating by an independent rating firm is likely to cost at least this much. In contrast, Mass-Save, the non-profit corporation in Massachusetts formed to perform energy audits, charged approximately \$5/rating to recoup its incremental costs for preparing a rating in conjunction with an energy audit for the Massachusetts HERS field test.⁽²⁾ Clearly, participation in a HERS program will be greater when the homeowner's cost can be kept low.

Real estate appraisers are also a possible rating group. An appraiser would normally rate a home when making an appraisal for a lending institution. The cost to make the rating will likely exceed the cost for an energy auditor or builder because an appraiser typically does not thoroughly inspect the energy-efficiency features of residential property. However, because the appraiser will be visiting the home with or without the rating, the incremental cost of conducting a rating will still be relatively low. An important difficulty with appraiser performed ratings is that the rating will generally not be performed until after price negotiations between buyer and seller are completed. Thus, the benefits accruing to buyers and sellers discussed in Section 2.1 of having rating information prior to price negotiation are significantly diminished. In addition, ratings will only be made for home buy/sell transactions where new bank money is loaned, since appraisers are not normally utilized when loans are assumed or in the case of owner financing.

3.0 IS LIABILITY A RELEVANT CONCERN?

The discussion in sections 1.0 and 2.0 identified a number of advantages and potential beneficiaries of HERS. In general, it appears that implementation of HERS can yield important energy conservation and consumer benefits and, depending on the delivery system available, at moderate cost. One concern that has been expressed by those who might implement a HERS is the fear of potential liability if a homeowner or other rating user alleges that the rating was negligently designed or performed and that damage was consequently incurred. An example of potential damage would be a homeowner who realizes less on the sale of a home because an allegedly faulty and negligent rating unfairly and incorrectly reduced the home's value. Another example would be a home buyer or tenant who buys or leases a home expecting the rating to reflect energy consumption and who later finds consumption to be higher than expected.

Institutions who may be involved in implementing HERS have expressed concerns about the liability issue. Real estate appraisers have expressed concern about liability if an appraiser rates a property as inefficient and the buyer is subsequently unable to secure financing.⁽²⁷⁾ Utilities have expressed concern about liability for their activities in carrying out the RCS program.⁽²⁸⁾ By analogy, they are likely to have some concern about conducting energy efficiency ratings. A related consideration is that, in most cases, it is likely that ratings will be subsidized or at least conducted at no profit by the rating sponsor. Under these conditions, the ability and willingness to absorb the risk of liability is reduced.

The principal objectives of this report are to examine these liability concerns, how liability might arise, and how the possibility of liability can be minimized, while still preserving the salutary attributes of a HERS. The issue of liability needs to be understood so that unfounded concerns are not permitted to defeat an otherwise beneficial HERS program or reduce the amount of information available to potential beneficiaries and users from a rating.

The issue of potential liability needs to be kept in perspective. While it is an important and legitimate concern, it should not be an overriding concern. During survey work conducted by PNL of existing HERS,⁽¹⁾ rating system

sponsors were asked whether the issue of liability was an important concern. Most said it was a concern, but not an overriding one. Only one utility, among about a dozen surveyed, could recall experiencing a loss related to their residential energy-efficiency ratings.⁽²⁹⁾ The utilities surveyed were generally part of the EEI/NEW program.

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4.0 WHO IS POTENTIALLY LIABLE?

There are three principal groups that are potentially liable for misapplication of rating systems: the individual rater, the organization sponsoring the rating system, and the rating system developer. There is also the possibility of indirect liability on the part of real estate agents, homeowners, and builders and architects.

4.1 INDIVIDUAL RATER AND SPONSORING ORGANIZATION

If the rater negligently performs a rating thereby harming a plaintiff, the rater is individually liable for his conduct. Often, however, a plaintiff injured by an employee will seek to place liability on the employer under the general principles of respondeat superior because the employer is in a better financial position to pay a judgment than an employee. The general rule is that the principal (employer) is liable for a tort⁽¹⁾ of the agent (employee) that is committed in the course of employment, even though the principal has not authorized the tortious conduct.⁽²⁾ A negligently performed rating would ordinarily be committed in the course of employment, and the doctrine of respondeat superior would apply. The rating sponsor would then be jointly liable with the individual rater.

The rating sponsor would not be liable if the rater could be classified as an independent contractor. The test of whether an employer-employee relationship exists rather than an independent contractor is whether the employer can exercise the right of control over the employee's activities.⁽³⁾ Because the rating sponsor will ordinarily be able and want to control how a rating is conducted, it is unlikely that a rater would be considered an independent contractor for the purpose of assigning liability.

4.2 RATING DEVELOPER

The greatest possibility of liability for a rating system developer would be a claim by the rating system sponsor that the rating was negligently formulated. The possibility that the rating system developer would incur liability to individuals is more remote. In this case an individual plaintiff would need

to show that the rating process was negligently formulated. This showing would be a heavy burden for an individual plaintiff, although a group of plaintiffs could conceivably bring a class action suit alleging such negligence. Often the rating sponsor and developer will be the same entity. However, liability can potentially extend to the developer even when the developer is not a sponsor and has no direct contact with rating users. The developer's liability for a negligently prepared rating system can extend to all who may foreseeably be injured.⁽⁴⁾ A homeowner monetarily injured by a faulty rating is probably a foreseeable plaintiff. Other injured parties such as lenders and home purchasers are also foreseeable, but more remotely. The rating system developer is thus potentially liable to third parties. Absolute rules are difficult to state, and liability would be determined on a case-by-case basis.

4.3 BUILDERS AND ARCHITECTS

Builders and perhaps architects may indirectly be subject to liability from the rating process. As home energy-efficiency ratings become better known, it is likely that some individuals having homes built will specify in their construction contract with a builder, design contract with an architect, or both, that the resulting home have a specified rating. When the home is ultimately rated, a builder or architect may incur liability to the homeowner if the rating is less than that called for in the contract. The issue has already arisen in more than one instance in the case of builders in the service area of the Greenville Utilities Commission in North Carolina.

4.4 HOMEOWNERS AND REAL ESTATE BROKERS/AGENTS

The possibility of indirect liability also exists when rating information is not disclosed or correctly conveyed to a potential home buyer or tenant. This situation might arise, for example, if a poor rating is not disclosed or is misrepresented by a homeowner or real estate agent to a prospective buyer. Nondisclosure when no inquiry about a rating is made is not a violation of federal law or the law in many states. The general rule, unless modified by statute, is caveat emptor - let the buyer beware. In some instances, however, nondisclosure could be a violation of a state or local statute or the state's

common law. Regulations issued under the Massachusetts Consumer Protection Act, for example, require disclosure of "any fact, the disclosure of which may have influenced the buyer or prospective buyer not to enter into the transaction."⁽⁵⁾ Nondisclosure of a poor energy-efficiency rating could subject a homeowner or real estate agent to potential liability under this requirement.

If a homeowner or real estate agent intentionally or negligently misrepresents the existence of an existing rating or the contents of the rating, the probability of liability is greater than in the case of nondisclosure. The basis for liability in this case would be fraud or violation of a consumer protection statute. Remedies available to a purchaser could include damages and/or rescission of the purchase contract (see Section 5.6).

5.0 GENERAL PRINCIPLES OF LIABILITY AND THEIR APPLICATION TO PARTICULAR HERS USES

This section examines general liability principles and how they might apply to implementation of a HERS. The topics covered are negligence, misrepresentation, concealment, violations of statutory duties, contractual liability, measurement of damages and the effect of statutes of limitations.

5.1 NEGLIGENCE, PROXIMATE CAUSE, AND FORESEEABILITY

The basis for any claim of liability for improper formulation of a rating system or improper performance of a rating will be that the defendant acted negligently. There are four classic elements that a plaintiff must show in a suit based on negligence.⁽⁶⁾ The plaintiff may recover only if:

1. the defendant was under a duty to the plaintiff to use due care,
2. the defendant was guilty of a breach of the duty,
3. the plaintiff has suffered damages, and
4. the breach of the duty proximately caused the damage.

The questions of whether the defendant was under a legal duty to conform to a standard of conduct to protect the plaintiff and the nature of any such standard thus become critical in determining whether liability exists.

In general, the courts have said that everyone has a duty to exercise that care which a reasonable man would exercise under similar circumstances. Professionals have a duty to exercise the skill and knowledge ordinarily possessed and exercised by members of the profession.⁽⁷⁾ For professions with a long history of negligence litigation, e.g., medicine, the courts have slowly evolved common law duties and standards of conduct. Such duties also exist for architects and builders and would be applicable in an action based in part on negligence claiming that a house was not built to the energy rating contracted for. No such duties and standards currently exist for individuals who formulate or perform energy ratings.

There are two reasons for the lack of court decisions regarding energy-efficiency ratings. One obvious reason for the lack of precedent is that energy ratings are relatively new. A second less obvious reason is that the

amount of damage suffered by a plaintiff from a faulty rating will usually be too small to justify the legal expense of taking a case to a court of record where the decision would establish a precedent and be accessible to legal researchers. The general American rule that each party to litigation pays his own attorney's fees regardless of who prevails is also a contributing factor. If legal action is brought, it would probably be in a court of limited jurisdiction, e.g., a small claims court, where cases are not reported. If an action were brought in a state court of record, it would likely be settled before trial; a case that did go to trial would be unlikely to be appealed, again because of the cost. At the state level only appellate decisions are available for review and study because trial court decisions are not printed in the case reporters. The financial disincentive to pursue cases involving energy ratings suggests that future court decisions are likely to appear in the case reporters very slowly. A thorough computer-assisted search of reported cases conducted in mid-June 1983 revealed no decisions in state or federal courts on the subject of energy-efficiency ratings or labels. The search covered not only rating/labels for buildings, but also automobiles and home appliances.

In spite of the lack of case precedent, it is possible to suggest several duties that a rating formulator or performer may owe the public. These duties can be postulated by examining duties that have evolved for related activities, such as building inspections and real estate appraising. These possible duties are discussed in Section 6.

As previously noted, the fourth element necessary for a negligence claim is proximate cause. There are two causation elements to consider in determining whether a plaintiff should be allowed to recover for alleged negligent conduct.⁽⁸⁾ The first and most obvious element is that the injury or damage must have been in fact caused by the negligent conduct. If cause-in-fact can be established, proximate (or legal) cause must then be shown before recovery can occur. Proximate causation is an elusive concept to pin down. In determining whether damage is proximately caused by a negligent action, courts are likely to consider a number of factors, including the following: 1) how remote the injury is from the negligence, 2) the relationship between the injury and the

culpability of the negligent party, 3) the extent to which the negligence bringing about the harm is extraordinary, 4) the reasonableness of placing the burden of recovery on the negligent party, 5) the extent to which allowance of recovery would encourage future fraudulent claims, and 6) whether allowance of recovery would lead to a situation where there is no sensible stopping point for future claims.⁽⁹⁾

It seems fairly clear that if a negligently formulated or performed rating causes a buyer to pay more for a residence than he otherwise would have, recovery of damages is possible. A plaintiff in this case, however, would have to clearly establish that the unexpectedly high energy consumption was due to the home's physical features and not his energy consumption habits. Liability is less clear when, for example, a lending institution suffers damage as a result of a negligent rating. A bank might conceivably incur damage in the following hypothetical manner. Suppose a bank lends more funds to a homebuyer than it ordinarily would because of the expectation that a high energy-efficiency rating will mean lower fuel costs and greater debt repayment capacity. It turns out that the rating was negligently performed and fuel costs are higher than expected. The buyer defaults on the loan. Home prices have declined since the time of purchase and the bank suffers a loss when the home is resold after foreclosure. Does the bank have a claim against the energy rater? There is no clear answer, but it is likely that the bank would have a difficult time recovering. The chief reason for their difficulty would be the problem of showing that the negligent rating was the cause-in-fact of the loan default. Other possible reasons for default include the energy consumption lifestyle of the homeowner, and a variety of other factors unrelated to energy, including changes in the homeowner's family size and makeup, and economic disruptions such as job loss. A second possible reason for difficulty is that the bank's damage may be considered too remote from the negligent conduct. This second reason raises the issue of foreseeability.

The issue of foreseeability is very much related to the issue of proximate cause. Both are gray areas of tort law in which there is no uniform agreement among courts. The general rule is that foreseeability of the injury is pre-requisite to liability.⁽¹⁰⁾ A defendant is only liable if the damage that

occurred as a result of his negligence could have been anticipated by a reasonable person in the defendant's position. Putting these general rules into practice is not always easy. Rating system developers, sponsors, and individual raters could certainly foresee that a particular rating will be used by one or more future buyers of a home. In addition, a rating system developer and sponsor could probably be expected to know that ratings might be used by lenders. They therefore could be liable to a financial institution that suffers loss because of a negligently designed or performed rating if the institution can establish the negligent rating as the cause of its loss. The Supreme Court of New York, Appellate Division, for example, recently held that a real estate appraiser could be found liable when its negligently prepared appraisal led to a financing party suffering damage.⁽¹¹⁾ An individual performing ratings, however, may very well not anticipate use by a lender unless this possibility were explained to him ahead of time.

5.2 MISREPRESENTATION AND DECEIT

The negligence theory discussed in Section 5.1 would primarily be used to support an allegation that a rating was negligently performed or that a rating system was negligently formulated. Other tort theories that can lead to liability are misrepresentation and deceit. These theories would ordinarily be used alone or in combination with the traditional negligence theory discussed in Section 5.1 when a homebuyer alleges damage because a rating was intentionally, negligently, or even innocently misrepresented to him.

Misrepresentation as a separate tort action concerns misstatements that result in monetary damage to a plaintiff.⁽¹²⁾ The misrepresentation can be intentional, negligent, or innocent. If it is intentional, the tort is generally based on the legal theory of deceit. The elements of a cause of action for each type of misrepresentation are somewhat different.

The elements of a cause of action based on deceit are:

1. a false representation of a fact,
2. knowledge or belief on the part of the defendant that the representation is false,

3. an intention to induce the plaintiff to act on the misrepresentation,
4. justifiable reliance on the misrepresentation by the plaintiff, and
5. damage to the plaintiff resulting from the reliance.⁽¹³⁾

Whenever a defendant intentionally misrepresents a rating to a buyer or tenant, the likelihood of liability will be high.

The test for negligence misrepresentation in the Restatement of Torts is that a defendant is liable if he supplies false information for the use of others in their business transactions that is justifiably relied upon and he fails to "exercise reasonable care or competence in obtaining or communicating the information."⁽¹⁴⁾ While the Restatement positions are generally given great weight by courts, a caveat by one commentator is that this test "does not state accurately the holdings of the cases and has little predictive value."⁽¹⁵⁾ Under the Restatement test, a homeowner or real estate agent who negligently relates false rating information to a prospective homebuyer or tenant could be liable.

Liability can also occur even if the misrepresentation is made innocently, i.e., when a home is sold and a rating is innocently but erroneously misrepresented.⁽¹⁶⁾ The theory is that even if the misrepresentation is innocent, a seller will be unjustly enriched if a buyer overpays for a home with a lower than expected energy rating. A buyer's remedy in this case is likely to be limited to the amount of money necessary to bring the home up to the rating that was represented by retrofitting energy conservation improvements. Recission of the purchase after a deed has been executed is unlikely. The possibility of recission after a contract of sale has been entered into but before the deed has been executed is somewhat more likely (see Section 5.6.3).

The common law of misrepresentation and deceit, and concealment and non-disclosure (discussed in the following section) has been affected by statute in many states. This impact is discussed in Section 5.5

5.3 CONCEALMENT AND NONDISCLOSURE

Both active concealment and nondisclosure of an existing energy rating can potentially lead to liability. The clearest case for liability would be where a real estate agent or homeowner actively conceals a rating by not producing it when asked or by representing that a rating does not exist when in fact it does.

The case for liability for simple nondisclosure of a rating is less clear; however, liability would still be imposed in many states if a buyer reasonably perceived greater energy efficiency than the rating indicates. The Restatement of Torts⁽¹⁷⁾ states the duty of disclosure in the following way:

One party to a business transaction is under a duty to exercise reasonable care to disclose to the other before the transaction is consummated... (e) facts basic to the transaction, if he knows that the other is about to enter into it under a mistake as to them, and that the other, because of the relationship between them, the customs of the trade or other objective circumstances, would reasonably expect a disclosure of those facts.

In other words, courts have imposed a duty to disclose important facts in business transactions if sellers know that the purchasing party is about to enter into the transaction in ignorance of important facts and if the purchasing party would reasonably expect disclosure during the bargaining process.⁽¹⁸⁾ An energy rating is arguably an important factor in a home sale transaction and a prudent seller or agent should thus disclose any existing energy rating known to them during the process of negotiation.

5.4 CONTRACTUAL LIABILITY

This section discusses two possibilities of liability related to the use of rating systems that are based on the law of contracts. The first possibility is a contractual remedy based on fraud in a home sale. The second possibility is use of a third party beneficiary theory by someone not a party to the sale transaction.

5.4.1 Claims by a Purchaser

All of the liability theories discussed in Sections 5.1-5.3 are based on tort law. When fraud has been committed in conjunction with a home sale, a buyer might also want to seek a remedy based on the law of contracts. A claim based on the law of contracts could be pleaded in conjunction with a tort claim or separately. The principal reason why a purchaser would want to assert a claim based on the law of contract is the possibility of rescinding the sale transaction. An action based on a tort theory may be limited to damages only. Another reason is that the statute of limitations (see Section 5.7) is typically longer for contract claims.

If a seller or real estate agent misrepresents a rating in conjunction with a contract for sale of a home, a remedy based on the law of contracts is possible. The misrepresentation can be either intentional (i.e. fraudulent) or innocent. The underlying theory for allowing a remedy is that a seller should not be permitted to unfairly enrich himself.

One commentator states that if the elements of a tort deceit action are present, rescission of a contract based on the misrepresentation will be possible. However, rescission may also be possible even if a deceit action cannot be maintained.⁽¹⁹⁾

For a plaintiff to prevail, a misrepresentation must be material. If the misrepresentation is intentional, even a slight misrepresentation (e.g., a house rated a "7" is stated to be an "8") can provide grounds for damages and rescission.⁽²⁰⁾ If the misrepresentation is made innocently, materiality is more important, and the above example would not likely provide grounds for rescission.

The general rule is that complete silence does not provide grounds for recovery based on contract law. (But see Section 5.3 for recovery on a tort theory and Section 5.5 for recovery based on violation of a statute.) Thus, in the absence of a statute or regulation, it is not a duty of the seller based on contract law to disclose the home's rating to a prospective buyer if the buyer makes no inquiry. Some courts have imposed a duty of disclosure when the defect is material and hidden from the purchaser.⁽²¹⁾ This exception would not

seem to be applicable to energy-efficiency features except in unusual circumstances. One possible example is that there may be a duty of disclosure if a home's energy conservation features were not built to code when the home was constructed.

5.4.2 Claims by a Third Party

In the United States, individuals or entities that are not party to a contract can assert a contractual remedy if it can be established that the contracting parties intended that a contractual right be created in the third party. If the parties so intended, the third party is referred to as a third party beneficiary. It is at least conceivable that a lending institution or a subsequent purchaser of a home who relied on a misrepresented rating to their detriment could claim third party beneficiary status and sue the original seller or real estate agent. The possibility of a successful claim on a third party beneficiary theory is remote because it will be very difficult to show the requisite intent by the contracting parties to benefit the third party.

Recovery by a third party based on tort law principles rather than contract is more feasible. The key elements for recovery on tort principles are foreseeability and proximate cause, both discussed in Section 5.1. If the third party plaintiff can establish that its injury was foreseeable and proximately caused by the defendant's act, then recovery is possible. Actions by the defendant that could lead to recovery include a negligently performed rating or a misrepresented rating. An important factor in any third party claim is likely to be the statute of limitations. This factor is discussed in Section 5.7.

5.5 VIOLATIONS OF STATUTES

This section covers two areas often covered by statute -- consumer protection and real estate licensing -- that can affect use of energy rating systems.

5.5.1 Consumer Protection Statutes

The focus of this subsection is on consumer protection statutes that are applicable to the sale and purchase of a home. Particular attention is given to the Massachusetts Consumer Protection Act. Consumer protection statutes

frequently go beyond the common (i.e. judge-made) law in establishing legal duties and remedies. In addition to consumer protection statutes, certain states have enacted statutes that codify what constitutes actionable fraud and misrepresentation in general.

The Massachusetts Consumer Protection Act prohibits any "unfair or deceptive acts or practices in the conduct of any trade or commerce."⁽²²⁾ Regulations under the Act issued by the State Attorney General state that an unfair or deceptive act is committed if a person "fails to disclose to a buyer any fact, the disclosure of which may have influenced the buyer or prospective buyer not to enter into the transaction."⁽⁵⁾ Both the sale and leasing of real estate are within the scope of the Act and regulations.⁽²³⁾ A successful buyer can potentially recover actual damages, attorney's fees, and, if the broker's or homeowner's violation was willful or intentional, punitive damages up to an additional two times actual damages.

Court decisions in Massachusetts have established three types of situations regarding unfair or deceptive practices.⁽²⁴⁾ These three situations can be applied to energy ratings and likely disclosure obligations of real estate brokers/agents and homeowners can be identified.

1. If a rating exists which a homeowner or agent has knowledge of, there is likely to be a duty of disclosure even if no inquiry is made by a prospective buyer. The statute is thus consistent with the common law policy favoring disclosure discussed in Section 5.3.
2. If a homeowner or agent makes no disclosure of a rating because of no knowledge of its existence, liability is possible if a rating actually does exist. The key inquiry a court would make here is whether a reasonable broker/agent should have inquired and discovered the existing rating. Whether or not nondiscovery is reasonable would likely depend on the ease of discovery of a rating. If ratings are stored and available from a central location, discovery is facilitated and liability is more likely. The burden of discovering an unknown rating on an owner selling his own home is likely to be less than a broker/agent because a homeowner is not in the

business of selling homes and, consequently, cannot be expected to exercise the same degree of care and diligence that a real estate broker does.

3. If an erroneous rating is disclosed, the seller and broker risk liability unless there are mitigating circumstances. A good faith belief in the representation is not a defense if the actual rating can be determined with certainty.

Consumer protection statutes exist in many states. It is beyond the scope of this report to examine their impact on HERS; however, rating system developers and users in a particular state should investigate whether the state has such a statute and how it might apply to energy-efficiency ratings. As the Massachusetts example suggests, the statutes can potentially affect the duties of discovery and disclosure and the remedies available to a housing consumer.

5.5.2 Real Estate Licensing Statutes

Real estate licensing statutes are also potentially applicable to misuse of an energy rating by a real estate broker or agent. All 50 states have acts to license brokers and agents. These acts generally set out duties that must be followed or the broker or agent can be subject to disciplinary actions. The duties are similar, but not uniform from state to state.

Commission of fraudulent acts or misrepresentation can subject a broker or agent to disciplinary proceedings. In the state of Washington, for example, a broker's or agent's license can be suspended or revoked for:

1. Knowingly committing, or being a party to, any material fraud, misrepresentation, concealment, conspiracy, collusion, trick, scheme or device whereby any other person lawfully relies upon the word, representation or conduct of the licensee;
2. Committing any act of fraudulent or dishonest dealing or a crime involving moral turpitude.⁽²⁵⁾

These duties provide one more reason, in addition to the possibility of damages discussed in the following section, why brokers and agents will want to truthfully disclose energy ratings to prospective buyers and tenants.

5.6 DAMAGES AND REMEDIES

This section discusses the damages and remedies that are potentially available to parties who allege injury because of misuse of a home energy rating. The most likely plaintiffs are homeowners whose home is incorrectly rated too low, homebuyers who purchase a home that is incorrectly rated too high, and homebuyers who purchase a home whose energy efficiency does not meet their expectation because of misrepresentation. Actions based on tort law and contract law are covered.

5.6.1 Compensatory Damages

The general purpose of awarding nonpunitive compensatory damages in actions based on negligence is to repair a plaintiff's injury or make him whole again as nearly as possible by an award of money. In the absence of an authorizing statute, attorney's fees are not recoverable. An award to an injured homeowner might be the difference between what he received for his home and what he would have received if a higher (and correct) rating had been assigned to his home. Stated another way, the damage is the difference between the fair market value of the property as rated and as rated correctly. A damage award to an injured buyer might be the capital cost to upgrade the energy efficiency of a purchased home to the higher rating that was represented to him and, perhaps, the incremental utility costs incurred. Nominal damages are ordinarily not awarded in negligence actions. The plaintiff must prove actual damages in order to succeed in his claim.⁽²⁶⁾

When a plaintiff is suing on the tort theory of misrepresentation, the courts have taken two approaches to awarding damages.⁽²⁷⁾ The majority of states apply the "loss-of-bargain" rule and allow the plaintiff to recover the difference between the actual value of what has been received and the value that it would have had if it had been as represented. This difference might include the cost to upgrade the energy efficiency of the house and the incremental utility costs incurred because of the misrepresentation. This approach is also the measure of damages in claims based on contract law. A minority of state courts apply the "out-of-pocket" rule, and allow the plaintiff the difference between the value of what he has parted with and the value of what he has received. Under this rule if a buyer pays \$50,000 for a house

represented as having a higher energy rating than it actually has, there is no damage unless he can show that \$50,000 exceeded the market value of the home as purchased.

5.6.2 Punitive Damages

Punitive damages are damages awarded to a plaintiff over and above full compensation for his injury.⁽²⁸⁾ They are given to punish the defendant and as a lesson and warning to him and others not to repeat the action. Punitive damages can be authorized by statute as the Massachusetts Consumer Protection law illustrates. They are also permitted as part of the common law in most states. Common law punitive damages are generally only awarded when the defendant's conduct is especially outrageous or malicious. Mere negligence would not be grounds for punitive damages, but deceit could be.

5.6.3 Rescission and Restitution

Rescission of the sales contract is a remedy available to a home buyer who is financially injured by an incorrect or misrepresented rating and sues under contract law principles. The buyer who succeeds in this claim is entitled to restitution, i.e., return of his down payment, provided he returns the home. The remedy of restitution is also potentially available to a plaintiff using a tort theory who alleges that a rating was misrepresented to him and that he was damaged thereby.⁽²⁹⁾

Whether or not a buyer named by a faulty rating would want to seek rescission and restitution would depend on several factors. If the buyer has changed his mind about the purchase for reasons unrelated to the rating, this remedy gives him a possible way out. A buyer in a jurisdiction which follows the "out-of-pocket" rule of damages may seek rescission and restitution because of perceived difficulty in proving damage. For buyers in "loss-of-bargain" jurisdictions, rescission and restitution are less attractive because of the availability of damages. Rescission may be even less attractive if the sale has already closed. In this case the paperwork and excise taxes in transferring the property back to the original owner can be significant. Moreover, the time involved in securing the home loan, the loss of loan origination fees, and possible prepayment penalties will discourage cancellation of the home financing.

An injured buyer may be able to recover these bank related costs and excise taxes in his request for damages, but this result is not certain.

5.7 STATUTE OF LIMITATIONS

In all states there are statutes of limitations that dictate when a legal action must be commenced to avoid being barred. The statutes will be helpful to rating system developers, sponsors, and individual raters concerned about liability for long past actions. For tort actions, the maximum period of time that can elapse prior to initiation of a claim is generally one to three years. The time is measured from the date of the action giving rise to the claim. The period is longer for claims based on contract law, generally four to six years. This longer period may be useful to an injured plaintiff who can file his claim on a tort or contract theory.

Identifying the time when the action giving rise to a claim occurs will not always be straightforward. If the action is the time when a rating is performed, the time is clearly the date of the rating. If the rating system developer is the defendant, the date is perhaps the date of publication of the rating system. If the system is updated or republished does the republication date become the new date for the statute of limitations? The answer is not clear.

5.8 SUMMARY

Section 5 has discussed general principles of liability and how the principles might be applied to particular HERS users. Table 1 indicates 8 actions that can potentially lead to liability, possible plaintiffs, the actors potentially liable, and the liability theories that can be used to support a claim.

The subjects of damages and the impact of statutes of limitation are also discussed. The general rule on damages is that the successful injured plaintiff can receive a monetary award that places him as nearly as possible in the position he would have been in had the injury not occurred. Statutes of limitations establish a maximum period before the end of which a claim must be filed in order not to be barred. The statutes will help to protect potential defendants from long past actions. The period is generally longer for actions based on contract law than tort law.

TABLE 1. Actions Potentially Leading to Liability and Possible Plaintiffs and Defendants

<u>Action</u>	<u>Possible Plaintiffs</u>	<u>Possible Defendants</u>	<u>Liability Theories</u>
1. negligently formulated rating system	sponsor, homeowners	rating developer	negligence
2. negligently performed rating	homeowner, buyer/tenant	rating sponsor individual rater	negligence
3. intentionally misrepresented rating	buyer/tenant	homeowner, broker	contract fraud action, tort deceit action, consumer protection statute
4. negligently misrepresented rating	buyer/tenant	homeowner, broker	negligence, consumer protection statute
5. innocently misrepresented rating	buyer/tenant	homeowner, broker	tort-misrepresentation and unjust enrichment, consumer protection statute
6. intentional nondisclosure of rating	buyer/tenant	homeowner, broker	consumer protection statute, deceit
7. negligent nondisclosure of rating	buyer/tenant	homeowner, broker	consumer protection statute, negligence
8. home not constructed to contracted-for rating	homeowner	architect, builder	breach of contract negligence

REFERENCES AND NOTES
(Sections 4 and 5)

1. A tort is a civil wrong for which damages may be recovered.
2. James, A. Dooley, Modern Tort Law, section 16.02, Callaghan and Co., Wilmette, Illinois.
3. Ibid, section 16.03.
4. Ibid, section 33.12.
5. Quoted in R. S. Kutner, "The Menace of Chapter 93A," baystate Realtor highlights, Massachusetts Association of Realtors, Waltham, Massachusetts, March, April 1983.
6. C. Morris, C. R. Morris, Jr. Morris on Torts, Second ed. 1980, p. 44, Foundation Press.
7. Restatement (Second) of the Law of Torts, section 299(A), American Law Institute Publishers, St. Paul, Minnesota.
8. Ref. 2, Section 8.
9. Ref. 2, Section 8.03.
10. Ref. 6, p. 162.
11. Chemical Bank v. National Union Fire Insurance Co., 425 N.Y.S.2d 818, (1980).
12. Ref. 6, p. 291
13. W. L. Prosser, The Law of Torts, 4th ed., 1971, p. 685, West Publishing Co.
14. Ref. 7, Section 552(1).
15. Ref. 6, p. 296.
16. Ref. 6, p. 298.
17. Ref. 7, Section 551(2).
18. Ref. 6, p. 309.
19. Williston on Contracts, Third Edition, Section 1487, Lawyer's Cooperative Publishing Co.
20. Ibid, Section 1490.

21. Ibid, Section 1498.
22. Massachusetts General Laws Annotated Chapter 93A, Section 2(a). Nearly all states have proscribed "deceptive" acts. Twenty-five states, including Massachusetts, take a broader approach and proscribe "unfair" acts as well as "deceptive" acts. Section 5 of the Federal Trade Commission Act also proscribes unfair or deceptive acts in activities affecting interstate commerce. See generally, D. Rothschild and D. Carroll, Consumer Protection Reporting Service, Part III, Chapter 4.03, CSG Press, Kensington, Maryland.
23. Commonwealth v. DeCotis, 316 N.E.2d 748, (1974).
24. See generally, Robert S. Kutner, "The Menace of Chapter 93A, Part I, II, and III," baystate Realtor hi-lites, Massachusetts Association of Realtors, Waltham, Massachusetts, February, March, April, 1983.
25. Revised Code of Washington, Chapter 18.85.230.
26. Ref. 6, p. 44.
27. Ref. 13, p. 734.
28. Ref. 13, pp. 9-11.
29. Ref. 13, p. 732.

6.0 DUTIES OF RATING SYSTEM PARTICIPANTS

The purpose of this section is to suggest some likely duties of rating system designers, sponsoring organizations, and individual raters. These duties need to be followed or at least considered to minimize the possibility of liability.

6.1 DESIGNERS

The most likely party to bring action against a rating system developer is the organization sponsoring the system. In some cases the developer and sponsor will be the same, but the system could also be prepared by a developer under contract. If a rating system is negligently prepared, the sponsor would likely have sufficient incentive and resources to pursue a legal remedy. Prior to bringing a legal action, the sponsor would likely seek to negotiate corrections and improvements to the system.

The likelihood that the designer of a rating system will incur liability to home sellers and buyers is not great. The principal reason is that it will be very difficult and expensive for an individual home seller or buyer to show that a rating system was negligently designed. If sufficient home sellers and buyers are economically injured by a rating system, they could conceivably band together and bring a class action suit against the developer.

The tipoff that a rating system was not properly formulated will be an extraordinary number of homes where the energy rating is not consistent with actual energy consumption observations. Discovery will be particularly easy if the rating system includes an estimate of energy consumption, costs, or both. Individual variations can be explained in a variety of ways, the most likely of which is that an individual's energy consumption lifestyle differs from the assumptions in the rating system model. If the rating system consistently estimates consumption incorrectly, however, the possibility of defects in the model formulation becomes very great.

The principal duty of a rating system developer is thus to design the rating system with reasonable care so that it is appropriate for the use intended.

6.2 SPONSORS

The principal duties of the rating system sponsor will be to select a rating system with reasonable care, to select the group(s) or individual(s) who conduct ratings with reasonable care and verify that they receive proper instruction and training, and to see that the rating system is fairly implemented. Careful attention to these duties is the best action a sponsor can take to reduce the possibility of liability. If the sponsor is also the rating system developer, the duties in Section 6.1 will also apply.

In some cases there may be more than one sponsor. For example, a state agency could have overall responsibility for a rating system with local responsibility assigned to a city or county government.

The duty to select rating groups and individuals with reasonable care will be especially important for a sponsor. If incompetent rating groups or individual raters are selected, liability for negligently performed ratings could come back to the sponsor. The sponsor is especially vulnerable because it will generally have the financial resources to pay any judgment, and will thus be an attractive defendant for aggrieved plaintiffs.

Another duty of the sponsor is to verify that there is a procedure to obtain a homeowner's consent before a rating is conducted. Raters entering private property without such consent could technically be guilty of trespass.

6.3 INDIVIDUAL RATERS

The principal duties of the individual rater are to inspect the house, to verify and collect the relevant data, and to perform the rating calculations in a reasonably competent manner. Real estate appraisers serve a function similar to raters and they have been found liable when they have not performed these three duties in a reasonably thorough manner. Although appraisers look at many other factors besides a home's energy efficiency, examination of some of the cases provides an instructive analogy to how liability might arise for a home energy rater. In one case an appraiser who did not discover termite damage was held liable.⁽¹⁾ In another case an appraiser made an error in estimating square footage in making an appraisal for a home seller. The property was sold

with the purchaser relying on the appraised valuation. The New Mexico Court of Appeals held that an action by the purchaser against the appraiser was permitted on either a negligent misrepresentation theory or a contract third party beneficiary theory.⁽²⁾ In a third case, an appraisal firm was found liable for costs attributable to a three-month delay caused by its double counting property tax benefits. The miscalculation resulted in an incorrectly high valuation of a commercial construction project.⁽³⁾

An energy rater cannot necessarily rely with impunity on data supplied by others that are used in determining the rating. Real estate appraisers, for example, have been found liable when they relied on and used data supplied by others that was later found to be inaccurate.⁽⁴⁾ It probably is reasonable for a rater to rely on past utility bills. It may not be reasonable, however, for a rater to rely on the unverified statements of a homeowner regarding his home's energy conservation features.

An energy rater will generally not want to make a determination that an energy conservation feature does or does not meet the applicable building code. An exception would be if the building inspector also performs ratings. The rater will generally have no authority to make such a determination. If an opinion as to compliance is offered, it should be clearly stated to be just an opinion. The rating sponsor may want to consider including a written disclaimer on the rating output form given the homeowner that the rating contains no implication that energy conservation features have been correctly installed or that such features meet the applicable building code.

7.0 MITIGATION OF LIABILITY

This section addresses steps that rating system participants can potentially take to minimize the possibility and extent of future liability. Possible steps include full disclosure of the rating system limitations, careful design of rating output, and establishment of a complaint procedure for homeowners dissatisfied with their home energy rating.

7.1 DISCLOSURE AND CAVEATS

Perhaps the most effective single thing that rating system participants can do to minimize future liability is to fully disclose the rating system assumptions and limitations. For the rating system developer this means fully explaining to the sponsor how the rating was developed; all assumptions used including weather, thermostat settings, what energy consumption items are included (e.g., water heaters), etc.; limitations in the energy consumption models used; the potential impacts of the energy consumption lifestyle of individuals; and the uncertainty in the output. All of this information should be given orally and in writing.

Full disclosure to the homeowner is especially important. Clearly, it is not appropriate to disclose to the homeowner the theory and details of how a rating is computed. It may be appropriate to disclose key assumptions, however. It is appropriate to disclose the uncertainty in the rating output and how the rating can be affected by such things as the homeowner's family characteristics and energy consumption lifestyle. This disclosure on the rating limitations should be in writing accompanying the rating, and also should be orally explained to the homeowner.

The requirements associated with use of automobile fuel economy figures illustrates one disclosure approach. The U.S. Environmental Protection Agency requires automobile manufacturers to include the following wording along with the vehicle's estimated fuel consumption on the window sticker:⁽⁵⁾

The estimated mileage for this model is to be used to compare cars of this model design with other cars. Your own mileage may be poorer depending on options, driving conditions, your driving habits, and your car's operating condition.

A rating sponsor could include comparable disclosure language in every home energy-efficiency rating it issues.

The Federal Trade Commission (FTC) requires the automobile manufacturers in any advertising concerning estimated mileage to make a clear and conspicuous disclosure that the estimated mileage "is to be used for comparison purposes, and that the actual fuel economy to be obtained by the consumer may be different and will depend upon the individual's driving speed, weather conditions and trip length."⁽⁶⁾ A rating sponsor could also require, as a condition of its contract with the homeowner, that the homeowner include a caveat comparable to the FTC requirement in any advertising that the homeowner does in selling or renting his home. A state real estate licensing and regulatory agency could also adopt such a requirement if experience proved it needed and desirable.

The rating sponsor will want to also consider including certain caveats about the rating in the rating information supplied to the homeowner. These caveats could include the facts that no determination of building code compliance is implied (Section 6.3), that data sources have or have not been independently verified (Section 6.3), and that the rating output may be disclosed to third parties (Section 9.0). It is good practice not to put disclosures and caveats in fine print that is easily overlooked or ignored.

Use of disclosures and caveats serves two principal purposes. First, it educates and informs rating system users about the process of computing a rating and the limitations of the process. Second, it helps to mitigate against future claims that the rating system was negligently designed or the rating negligently performed by pointing out the limitations of the whole rating process and the importance of assumptions and individual energy consumption habits.

7.2 SELECTION OF RATING OUTPUT FORMAT

A rating designer and sponsor have a variety of choices for the format of the rating output.⁽⁷⁾ The simplest output is simply a certification that a home is energy efficient. A somewhat more detailed output would assign homes to a limited number of broad categories, e.g. "efficient", "average" or "inefficient." A more sophisticated approach would assign a rating based on a

sliding scale, e.g., 1 to 10. Finally, an estimate of energy consumption, cost, or both can be included with the rating.

Liability exposure increases with the amount and specificity of information included in the rating. This fact shouldn't necessarily be used to minimize or generalize the rating information conveyed because both efforts would reduce a rating's value to the user and diminish the usefulness of the whole rating system. Nevertheless, if the sponsor is seriously concerned about liability, the output can be structured to minimize the possibility. One obvious option is to use broader categories, e.g., rate homes on a scale of 1 to 5 instead of 1 to 10. A second approach would be to provide the homeowner an uncertainty band on a rating and associated estimates of energy consumption and cost. Thus a home might be rated a 5 to 7 instead of a 6, and estimated annual fuel costs as \$1500 - \$2500 instead of \$2000.

7.3 COMPLAINT PROCEDURES

Another possible means for a rating sponsor to minimize the possibility of future liability is to establish a formal complaint procedure for homeowners who feel their homes have unjustifiably received a low rating. After such a complaint, the home could be rerated. To discourage frivolous complaints, homeowners could be billed for the actual costs of rerating when the two ratings are the same. The sponsor could absorb the cost if the second rating differs from the first.

The complaint procedure could also be conceivably opened to home purchasers who contend they were monetarily damaged when they purchased a home with an erroneously high rating. The sponsor will want to give this possibility serious thought, however, before introducing it. The sponsor will not want its complaint procedure to encourage claims by home purchasers that the sponsor is liable by the amount the purchaser overpaid for a home because of the allegedly erroneously high rating. It has been estimated that an energy-efficiency rating can easily influence the value of a typical house by plus or minus \$2000.⁽⁸⁾

7.4 LANGUAGE LIMITING USE OF RATING

Another step a rating sponsor could take to minimize the possibility of future liability would be to include language on the rating output form limiting use of the rating. Such language might limit use to the homeowner only or perhaps include other parties such as a financing institution or tax assessor. The Society of Real Estate Appraisers, for example, suggests that appraisers consider including the following two clauses in their appraisal reports:⁽⁹⁾

Possession of this report, or a copy thereof, does not carry with it the right of publication. It may not be used for any purpose by any person other than the party to whom it is addressed without the written consent of the appraiser, and in any event only with proper written qualification and only in its entirety.

This appraisal report has been prepared for the exclusive benefit of (insert name of client), and is subject to the assumptions, conditions, and limitations agreed upon by (client) and (appraiser). Any third party who uses or relies upon information contained in this report does so at his own risk.

Although the use of language limiting use of the rating by others can create a presumption that any such use is at the user's own risk, it is not recommended that a rating system sponsor use this approach for two reasons. The most fundamental reason is that such language is inconsistent with the purpose of ratings. Ratings are performed to get energy-efficiency information to housing consumers, to aid the incorporation of energy-efficiency information into market value, to facilitate the marketing of energy-efficient buildings, and ultimately to achieve residential energy conservation. All of these purposes will be frustrated to some extent if use of ratings by third parties is limited by the rating sponsor.

A second reason not to include limiting language is that the language may not be effective anyway. If the rating sponsor knows that the homeowner intends to transmit the rating information to third parties, language limiting use by such third parties will not necessarily protect a sponsor from liability for a negligent rating.⁽¹⁰⁾ The position expressed in the Restatement of Torts is that such language will not provide protection in this situation.⁽¹¹⁾

7.5 MALPRACTICE INSURANCE

The rating sponsor who is seriously concerned about the possibility of liability for negligently performed energy ratings can consider the purchase of malpractice insurance. To make this purchase decision, the sponsor will want to compare the frequency and magnitude of potential claims against the insurance premium. This comparison will be difficult to make, principally because there has been so little claim experience involving energy ratings. The lack of experience will make it difficult for a sponsor to estimate the magnitude of potential claims and for an insurance company to estimate required premium revenue.

The alternatives to malpractice coverage are to function without insurance or to self-insure with a separate fund designated for potential liability claims. Before selecting the insurance option, a sponsor may want to try one of these alternatives for as long a time as necessary to gain sufficient knowledge of the extent of liability claims to provide a basis for a decision on insurance.

REFERENCES AND NOTES
(Sections 6 and 7)

1. Walker v. Gordon, Superior Court of State of Washington (1964), discussed in J. P. Messina, "Real Estate Appraisers and the Problems of Malpractice: An Overview," prepared for the Society of Real Estate Appraisers, Chicago, Illinois, May, 1977.
2. Stotlar v. Hester, 582 P.2d 403, 1978.
3. Breckenridge Hotels Corp v. Real Estate Research Corp., 452 F. Supp. 529, (1978).
4. Messina, Ref. 1, p. 8, 15. Hardy v. Carmichael, 207 Cal. App. 2d 238, (1962).

Peter J. Mastaglio, "Real Estate Appraisal Malpractice: Liability and Damages," New York State Bar Journal, p. 8, January 1982.
5. 40 C.F.R. 600.307-81(b)(2).
6. 16 C.F.R. 259.2(a)(2).
7. A discussion of output possibilities is at pages 1.4 - 1.5 of P. L. Hendrickson et al., Overview of Existing Residential Energy Efficiency Rating Systems and Measuring Tools. PNL-4359, October, 1982. A discussion of the process used to select an output format for the Massachusetts HERS pilot project is in Section 2.0 of A. Ackerman et al., The Massachusetts Home Energy Rating System Project, PNL-4763, August, 1983.
8. A. H. Rosenfield, B. S. Wagner, "Technical Issues for Building Energy Use Labels," LBL-14914, August, 1982, Lawrence Berkeley Laboratory, Berkeley, California.
9. Messina, Ref. 1, p. 20.
10. Ibid., Ref. 2.
11. Restatement (Second) of Torts, section 552, American Law Institute Publishers, St. Paul, Minnesota.

8.0 POSSIBLE LIABILITY DEFENSES

This section discusses three defenses that are potentially available to a rating system participant who has been named as a defendant in a damage claim. These defenses are the possibility of liability immunity for government entities, contributory negligence, and the inexactness of the rating science.

8.1 IMMUNITY OF GOVERNMENTAL ENTITIES

In many cases the sponsor of a rating system will be a governmental entity. In the absence of a statute authorizing tort actions, there is no tort liability for states or their subdivisions; all states have given consent to some extent, however. Until very recently these consent statutes were construed very strictly in favor of the state. If a state legislature chose to do so, energy rating activities of government entities and even private parties could be made immune from liability by statute.

Even with liability consent statutes, courts have used two doctrines to distinguish liability claims against states and their subdivisions. One doctrine involves the distinction between governmental planning and policy functions on one hand and operational functions on the other hand. The state, its subdivisions, and governmental employees are generally not liable for activities found to be of a planning or policy, i.e., governmental, nature, but can be liable for operational, ministerial, or proprietary functions. The second doctrine involves the distinction between public duties owed to the public in general and special duties owed to an individual or an identifiable class of individuals.

The state of Florida follows the policy-operational distinction. The test was applied in a recent case where the plaintiffs alleged that a municipality should be liable because its negligent building inspections contributed to the collapse of a roof at a condominium.⁽¹⁾ The Florida Court of Appeal found that building inspection was an operational activity and that the city could be found liable. By analogy, a municipal employee who conducts a negligent energy rating in Florida could subject himself and the municipality to liability.

The public duty doctrine involves the notion that the state is not liable to an individual member of the public if the duty allegedly breached was owed instead to the general public. The public duty doctrine is currently followed by a majority of states, and has generally provided a successful defense for governmental entities in cases involving housing inspections.⁽²⁾ By analogy, it could also apply to energy ratings. The reasoning is generally that building codes and inspections are intended to protect the general public and to provide a means for someone else, e.g., the building owner, to resolve defects. The doctrine has recently been abandoned in a minority of states.⁽³⁾ The Alaska Supreme Court concluded that it is in reality a "duty to all, duty to no-one" doctrine. The public duty doctrine comes down to a policy decision that legislatures and courts must make. With regard to energy ratings, a governmental entity might argue that conducting ratings is a public service, that no duty is owed to an individual homeowner, and that if the municipality incurs liability it will be discouraged from conducting ratings. A plaintiff might argue, however, that if the governmental entity is going to conduct ratings, it has an obligation to perform them in a careful manner.

If a plaintiff is injured by a negligent rating performed by an employee of a governmental entity, he can bring his action against the employee, the governmental entity, or both. The governmental entity is potentially liable under the doctrine of respondent superior discussed in Section 4.1. An action against the employee is possible even if the governmental entity is protected by sovereign immunity.⁽⁴⁾

8.2 CONTRIBUTORY NEGLIGENCE

Contributory negligence is a doctrine that bars a plaintiff's recovery if he is also guilty of negligence that was a proximate cause of his injury. It is difficult to predict in advance how contributory negligence might occur, but one example would be if a homeowner negligently supplied misinformation to a rater regarding his house and thus contributed to an incorrect rating.

In a minority of states, a plaintiff guilty of contributory negligence is completely barred from recovery. The majority of states have adopted the

doctrine of comparative negligence whereby a negligent plaintiff's potential recovery is reduced in proportion to his negligence, but not barred.⁽⁵⁾

8.3 INEXACTNESS OF RATING SCIENCE

Another possible defense that a defendant accused of a faulty rating may wish to raise is the inexactness of the rating system. The defendant might argue that he acted perfectly reasonably and that he exercised the skills and knowledge normally possessed by energy raters. The damage caused by the faulty rating, he might argue, was caused by the inexactness and uncertainties in the rating science.

This defense will be a tricky one to use in at least two respects. First, it appears that a carefully designed rating system can predict energy consumption reasonably closely. In the recent Massachusetts pilot project, it was shown that estimates can potentially come within 5% of actual energy use on average.⁽⁶⁾ Second, unless the defendant has warned the homeowner of the uncertainties in the rating process, it will be relatively easy to foresee how a homeowner or homebuyer would rely on a rating. If the homeowner is warned ahead of time by appropriate written and oral caveats (See Section 7.1), the likelihood of a plaintiff filing a claim is reduced. Similar reasoning applies to a warning that the plaintiff's energy consumption lifestyle or family characteristics can cause a discrepancy between the rating and observed energy consumption. If appropriate caveats are included with the rating, it will be difficult for a plaintiff to allege that the defendant was negligent, and it will be unlikely that a damage claim will be filed.

9.0 PRIVACY AND CONFIDENTIALITY ASPECTS OF RATINGS

There are possible instances where issues of privacy and confidentiality regarding energy ratings may arise. For example, if energy ratings are to be most effective, it will be desirable for the rating sponsor to retain files on homes that have been rated. If a prospective buyer of a home that has been rated requests the rating information, can the information be disclosed without violating the privacy of the homeowner? Another example is the case of a homeowner who receives a low rating on a home. If the home is listed for sale with a broker, can the broker or agent disclose a rating even if the homeowner asks that it be kept confidential? For maximum effectiveness of a rating system, full disclosure is desirable in each of these examples. With appropriate advance notification to the homeowner of the possibility of disclosure, it appears that disclosure can occur without fear of liability.

The common law recognizes at least four categories of invasion of privacy. The category with the greatest possibility of application to disclosure of energy ratings is "unreasonable and unwanted publicity given to the plaintiff's private life or public disclosure of embarrassing private facts about the plaintiff."⁽⁷⁾ The publicity or disclosure must be to the public in general, i.e., a large number of persons as opposed to one individual or a few.⁽⁷⁾ This limitation effectively relieves rating sponsors and brokers/agents from liability for invasion of privacy with the possible exception of a case where a broker places a newspaper advertisement that discloses a low rating on a home. Since a broker would be very unlikely to place such an advertisement because it would more than likely deter rather than attract buyers, the probability of liability is low.

To maintain an invasion of privacy action, the facts disclosed must be "offensive and objectionable to a reasonable man of ordinary sensibilities."⁽⁸⁾ A good argument can probably be made that an energy rating, no matter how low or poor, would never come within this definition and, consequently, that disclosure would not give rise to possible liability.

Statutes also provide some privacy protection. The Federal Privacy Act of 1974, for example, restricts the disclosure of records about an individual by

federal agencies.⁽⁹⁾ This Act is unlikely to impact disclosure of energy ratings because rating data will ordinarily not be developed or retained by a federal agency. Moreover, rating data are arguably information about residential buildings, not about individuals. Certain states also have privacy statutes that should be consulted.⁽¹⁰⁾

The right to confidentiality is a developing common law right that is relatively new. It requires balancing of the following factors:⁽⁷⁾

1. Does the plaintiff have a legitimate expectation that the information will not be disclosed?
2. Is disclosure required to serve a compelling state interest?
3. If disclosure is necessary, will it occur in the least intrusive manner?

Application of the three factors appears to favor disclosure of energy ratings. For factor one, the potential plaintiff can be given an expectation of disclosure if he is told ahead of time that the rating information will be disclosed upon inquiry. This disclosure can possibly be put in a consent form that a homeowner is asked to sign prior to a rating. A real estate broker can also explain the need for disclosure at the time a home is listed for sale. This need can be defended, in part, because of a broker's disclosure obligations under state licensing laws or a consumer protection statute. For factor two, disclosure is arguably required to serve a compelling state interest, that interest being energy conservation. For factor three, if disclosure is only made to potential home buyers and renters and not to the general public it should not be considered intrusive. In summary, it does not appear that disclosure of an energy rating need violate a homeowner's right to confidentiality.

Some energy rating sponsors will undoubtedly not want to disclose rating results because of possible liability, the difficulty of obtaining homeowner consent, or perhaps the chilling effect that request of a blanket disclosure release would have on the demand for ratings. Some utilities will currently not disclose the results of residential energy audits for one or more of these reasons. There is nothing in the DOE/RCS regulations⁽¹¹⁾ to prohibit disclosure. Nevertheless, for a rating system to operate most effectively, full

disclosure should be the policy to the extent possible. Full disclosure will aid the incorporation of energy efficiency into market value and encourage energy conservation, the two basic goals of a rating system.

REFERENCES AND NOTES
(Sections 8 and 9)

1. Trianon Park Condominium Association v. City of Hialeah, 423 So.2d 911, (1983).
2. "Municipal Liability for Negligent Building Inspections -- Demise of the Public Duty Doctrine," Iowa Law Review, vol. 65, pp. 1416, 1428, (1980).
3. E. g., Adams v. State of Alaska, 555 P.2d 235, (1976).
Wilson v. Nepstad, 282 N.W.2d 644, (Iowa 1979).
4. Civil Actions Against State Government, section 2.2.3, Shephards/McGraw-Hill, Colorado Springs, Colorado.
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ACRONYMS

BPA - Bonneville Power Administration
C.F.R. - Code of Federal Regulations
DOE - U.S. Department of Energy
EEI - Edison Electric Institute
HERS - Home Energy Rating System
LBL - Lawrence Berkeley Laboratory
NECPA - National Energy Conservation Policy Act
NEW - National Energy Watch
PNL - Pacific Northwest Laboratory
RCS - Residential Conservation Service
TVA - Tennessee Valley Authority
U.S.C. - United States Code

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