



Mold: An American problem, or a worldwide problem?

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«Insurance policies, both personal and commercial, do not normally cover mold as an insured peril. The problem arises when mold ensues from a covered loss.»

The problem is most acute in southern States where heat and humidity contribute to it. Nonetheless, cases of mold have been found in New York, Connecticut and other States across the country.

In addition to the direct impact felt by property owners and insurers, the indirect impact is being seen at the economic level. For example, in some areas of the country mortgage lenders have withdrawn commitments when they learned insurance was no longer available, and homeowners have found that they cannot sell their property once mold arises. These events bring serious financial problems for those affected. They also bring pressure on local, State and Federal governments to establish standards to cope with the myriad problems arising from this menace.

Is this a problem that threatens insurance markets in other countries? Let's look at some of the facts and issues that have led to the problem in the U.S., and then decide.

WHAT IS MOLD AS IT IS USED IN THIS ARTICLE?

As characterized on the NAII (web site www.naii.org), most interior mold is a byproduct of water reacting with modern construction materials such as drywall paper, carpeting, wall-paper backings and particle-board. Although the existence of the simple fungus has been documented since biblical days, modern structures, which are sealed to keep in heat and air conditioning, encourage the growth of mold, and mold feeds on materials such as drywall paper used in some modern construction.

MOLD IN INSURANCE POLICIES

Insurance policies, both personal and commercial, do not normally cover mold as an insured peril. The problem arises when mold ensues from a covered loss. The most common example would be a water pipe leak that is not dealt with soon

A new phenomenon has appeared in the U.S. insurance market over the last several years: *Mold damage*. This has been a sudden and unexpected development that has roiled the insurance industry, affected relations between insurers and insureds, and caused the construction industry to re-examine some of their building practices.

ESSENTIAL CHARACTERISTICS OF THE MOLD

1. Mold is one type of fungus.
2. Mold occurs normally in nature and is often beneficial.
3. There are over 100,000 types of mold, of which 10 are seen as toxic molds and can lead to serious health problems.
4. Not all molds causing property damage are claimed to be toxic.
5. The publicity given some "high profile" insurance cases has led to overreaction.
6. There are no sets of official standards in the U.S. relative to this problem. Examples of standards that would be helpful are: what is an acceptable level of mold in a home, commercial space or public building, or what are appropriate standards for remediation?



enough, or not dealt with adequately. A sudden and accidental water pipe leak would usually be covered under policies in the U.S. If there is coverage for the leak, and if the mold develops from the leak, it has been the normal practice to include the mold damage and repair in the loss adjustment. The problem becomes more complex when certain types of especially aggressive molds begin spreading to the rest of the building; one can begin with a minor water leak and end with remediation expense for the entire building.

There are also liability issues. For example, consider the case of an insured who has a water pipe leak in his condominium unit while he traveling away from home. Under the right dampness and humidity conditions, mold could easily develop. If it is not repaired in a timely manner and mold develops, it can spread to other areas in the building or even to the entire building. This can be a very significant loss; certainly a loss not previously contemplated under the Personal Liability Policy.

WHY HAS MOLD SPRUNG SO SUDDENLY INTO THE AMERICAN PUBLIC'S EYE?

While there has been an increasing occurrence of mold, particularly in dwellings in hot and humid areas, the public awareness has more of its roots in publicity surrounding a few well-known lawsuits. Among the better known is the Ballard case, in which a jury awarded USD 32.0 million (EUR 28.54 million) to a Texas family which had to abandon their mansion because of mold. The award was for USD 4.0 million (USD 3.57 million) property damage,

and USD 28.0 million (EUR 24.97 million) for punitive damages. The public hears and sees: «USD 32.0 million» and «Mold». But the claim was based on the premise that the insurer did not repair water leaks at the house quickly enough, so that the mold was able to spread. Yes, it is true that it was mold, but more correctly 'mold not attended to', or 'mold inadvertently left to grow'. Thus the majority of the loss was really a secondary occurrence, namely, 'the failure to act', that transformed what was probably a minor remediation loss and turned it into a total building loss. (Recently, an appellate court reduced the award to USD 4.0 million -EUR 3.57 million- while upholding the jury's conclusion.)

WHY ARE THERE MORE MOLD CASES NOW THAN, SAY, 30 YEARS AGO?

One has the sense that this is a new phenomenon. What then has contributed to the sudden rise of it? The prevailing opinions are that new developments in construction are the main causes, such as:

- tighter building designs responding to demands for better heating and air conditioning efficiency,
- changing construction techniques,
- use of lighter building materials that mold feeds on, and
- the willingness to build near wetlands or bodies of water (while using these tighter designs and lighter materials).

HAVE INSURERS CONTRIBUTED?

In some ways, insurers have exacerbated the basic problem.

The insurers were slow to recognize the problem as various molds invaded these tighter buildings. Further, the industry was slow to realize the critical importance of quick damage repair and immediate and thorough remediation. The latter caused damage to be more severe and extensive. In addition, over the past few decades there has been a broadening of policy terms. Broadening of coverage is certainly a worthy objective, but it does lead to continual broadening of interpretations – very often to the surprise of the form designers.

All of these elements have contributed to the evolving situation which in the last 10 years has led to major property losses, and in some cases, personal injury losses.¹

HOW ARE INSURANCE COMPANIES DEALING WITH THIS PROBLEM?

Not surprisingly, insurers are finding alternate ways of dealing with this issue, and their efforts vary by company and State. The most common ways are:

- limiting the loss,
- absolute exclusion, and
- selling specific mold insurance.

Loss limitations

The most prevalent alternate way of dealing with mold is to write loss limitations into the policy to cap the amount that can be claimed for repair and remediation of mold damage ensuing from a covered loss. Such limitations could in the case of property coverage be caps in the USD 10,000 (EUR 8,918.2) to USD 50,000 (EUR 44,591) range, or 10% of the sum insured; and amounts

¹ There have been personal injury claims from some property owners. The health problems affecting these people are alleged to have come from some toxic molds that developed when remediation efforts were delayed for long periods.



such as USD 300,000 (EUR 267,546) in the liability coverage. While such limits will probably be adequate for many losses, in the extreme case where, e.g., a home has become uninhabitable, the loss limitations will be woefully inadequate.

Absolute exclusion

Another approach to dealing with the problem is to seek approval to exclude *any* type of mold loss, but State regulators are resisting. While the exclusion of mold as a peril is reasonable, it would seem that elimination of all coverage would be an overreaction. This is a drastic step; the potential personal and commercial financial impact from a lack of coverage could cause significant economic harm.

Providing separate mold insurance

In some cases insurers are offering specific mold coverage as an endorsement or as a separate policy. This would be similar to earthquake and flood insurance; one would have to purchase the coverage in order to have protection. This brings its own set of problems, such as adverse selection. Nevertheless, this solution has value for those who live in an area with a mold history because they will be able to buy protection. Insurers, for their part, will have the opportunity to underwrite and price the risk. Such a development would be welcomed by property owners who are finding it difficult to find mortgages, to get bank loans for improvements, or even to sell their property. Just by qualifying for coverage, the insured will have stabilized what might other-

wise have been a threatening financial situation.

In the absence of mold standards from the Federal government, the insurers are working with State governments to establish mold standards. The eventual development of effective mold standards could be very beneficial to architects, contractors, risk managers, remediation experts and lawyers.

THE NEXT ASBESTOS?

As stated in Fortune Magazine (May 28, 2002): «So will mold turn out to be another asbestos? Probably not. While asbestos litigation is predicted to cost insurers and manufacturers USD 60 billion (EUR 52,2 billion) to USD 70 billion (EUR 60,9 billion), the tally for mold is likely to be far lower. And, unlike toxic asbestos, barely half a dozen of the thousands of mold varieties are believed to cause health problems.»

Although it makes nice headlines, mold is not lurking asbestos. As one can see from much of the above material, mold is not a hidden loss that is going to spring suddenly upon the world and continue surprising us for many years. This is a relatively normal phenomenon that will be controlled as we learn more about how to be on guard for its presence. As underwriters become more aware of it, as there is more effective underwriting of risks in exposed areas; as records are maintained of infected properties, and as claims adjusters are more alert in their loss assessment not only of the immediate damage but the need for, and extent of, remediation work required. Plans are already progressing for towns to adjust their building codes, and for architects/builders to adjust their building practices.

MIGHT THIS BE A PROBLEM FOR OTHER COUNTRIES AS WELL?

Mold is everywhere. Clearly we know that mold grows everywhere and that some of these molds are toxic. If the insurance industry in your country has significant exposures in hot and humid areas, then there is a good possibility that there will be mold damage.

Here are some questions you will have to weigh as you consider whether this phenomenon could occur in your country:

- Do your property policies cover costs of repairing mold damage caused as a result of an insured loss?
- Does that coverage extend to remediation of the property?
- What happens in your system if an adjuster, who has not been properly trained about the nature of mold, pays to repair a water damage loss but fails to take remedial steps to clean up the toxic mold?
- Have lighter weight modern construction methods become prevalent in your country?
- Have tighter construction techniques led to 'sick' buildings?

This phenomenon, like others that suddenly appear, seems to have passed through its growth phase. There is reason to think that the impact from new losses and lawsuits will begin to diminish, and to hope that the problem will eventually be dealt with in less dramatic ways as all parties adjust their practices and procedures. Progress will become more evident as accelerated steps are taken to educate the public, to train insurance underwriters and claims personnel, and to adjust building codes. The worst may be behind us. ■



FOR FURTHER INFORMATION...

Benfield Blanch. "Mold: Issues for Insurers" 2001

<http://www.benfieldgroup.com>

Environmental Protection Agency

<http://www.epa.gov/iaq/molds/moldresources.html#Large%20Buildings%20and%20Mold>

National Association of Independent Insurers

<http://www.naii.org/sitehome.nsf/IndustryIssuesMold?OpenPage>

National Association of Mutual Insurance Companies

<http://www.moldupdate.com/>

Texas Department of Insurance

<http://www.tdi.state.tx.us/commish/mold.html>

Building Industry Site

http://www.housingzone.com/forums/mold_insurance/

Insurance Information Institute

<http://www.iii.org/media/hottopics/insurance/mold2/>

American Society of Heating, Refrigerating and Air-Conditioning Engineers

http://www.ashrae.org/NEWS/2003_mold-maint.htm