

# Commercial Insurance Update

Topics Affecting Buyers of Commercial Insurance

MSP C 06/2003 – “Mold Is a Four Letter Word”

June, 2003

## Mold Is a Four Letter Word

It seems you can't open an insurance trade publication these days without reading a horror story about toxic mold – “the next asbestos,” some are calling it. Because of this, we are starting to see mold exclusions appear in a number of different types of insurance policies.

Is this a rational response by the insurance industry to what some perceive as an uninsurable exposure, or is it an overreaction?

When you read things such as the examples that follow, you might side with the insurance industry:

- Farmer's Insurance Group paid a \$32 million dollar judgment to a Houston-area homeowner who claimed her insurance company failed to identify and remedy a mold problem in her home.
- Celebrity Ed McMahon filed a \$20 million lawsuit after mold caused by a water pipe leak allegedly killed his dog and made him and his wife ill.
- Erin Brockovich, the activist portrayed on screen by Julia Roberts, filed a \$600,000 homeowner's claim and became an active crusader against the danger of “toxic mold.”
- A \$400 million class-action lawsuit has been filed against the New Museum of Contemporary Art of New York alleging that several workers were exposed to mold and are suffering exposure-dependent immune dysfunction.
- The Hilton Hawaiian Village, one of the largest hotels in the world, closed down more than 450 guest rooms in the newest of its six towers and

is spending \$10 million to eliminate potentially dangerous mold – even though not a single guest reported health problems.

In all, the Insurance Information Institute (III) estimates that mold claims cost insurance companies more than \$1.2 billion in 2001 – and that figure has been rising rapidly. The III claims that 10,000 mold-related lawsuits were pending in 2002, representing a 300% increase over 1999 numbers. Virtually any member of the building industry – architect, engineer, contractor, owner and material supplier – faces exposure to mold-related claims.

**Mold** (Continued on page 2)

### In This Issue:

<b>Mold Is a Four Letter Word</b> .....	1-4
<b>Reduce Your Total Cost of Risk: Strategies for Winning</b> .....	4-5
<b>Cavnagac Staff Shines This Summer!</b> .....	5

Published by

**Cavnagac & Associates**

INSURANCE BROKERS  
License No. OA99520

1230 Columbia Street, Suite 850  
San Diego, CA 92101-3547

Phone: 619-234-6848 ✧ Facsimile: 619-234-8601

Web Site: <http://www.cavnagac.com>

## What's All the Fuss About?

Obviously, mold is nothing new. The Centers for Disease Control (CDC) estimates that there are up to 300,000 species of mold and they exist virtually everywhere in North America. A type of fungus, mold thrives in warm, humid environments and spreads by releasing airborne spores, similar to a plant spreading its seeds.

Some molds are considered toxic. Indeed, there are demonstrated cases of livestock dying after eating quantities of mold-laden grain. However, there is much debate whether toxic molds inside homes or buildings can cause serious human health problems.

According to the CDC, most documented cases of such health problems involve people who ate moldy food. Other studies have concluded that there is no evidence that toxic mold in levels found in homes and offices can cause chronic or life-threatening health problems.

Still, that is not to say that mold is not a viable health hazard. It's just that the so-called "toxic molds" are typically not the culprit. A large number of molds are "allergenic." That is, they release spores that cause allergic reactions and can trigger more serious health conditions such as asthma and sinus infections. And individuals with compromised immune systems are particularly susceptible to lung infections that can be caused by inhaling mold spores.

So why is mold, which has been around throughout history, suddenly such an issue? The answer depends on whom you ask.

Many will point to plaintiffs' lawyers, and the media frenzy surrounding the \$32 million jury award in Texas, and the celebrity cases of Ed McMahon and Erin Brockovich. As mentioned before, mold is already being called the "next asbestos" in some legal circles, with the favorite slogan of many plaintiff attorneys now being "mold is gold."

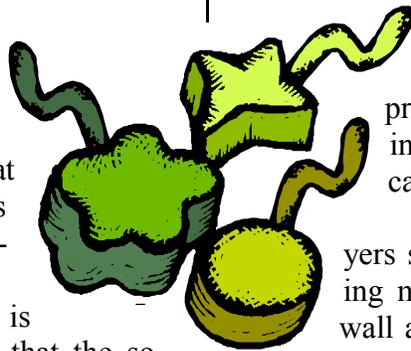
Indeed, there is money to be made from mold, and cottage industries have already sprung up surrounding mold litigation. Testing, inspection and

extraction has become big business, as have industrial hygienists and other mold consultant services.

Others will point to building owners as a source of the problem. Older buildings with leaky plumbing or poorly inspected and maintained HVAC systems are major contributors to the problem.

Ask anyone involved with a major building renovation project and they will likely have some horror stories regarding the black slime they have discovered under floorboards and inside walls. Another major culprit is poor quality construction. Some contractors use cheap, cost-cutting materials or fail to provide proper water barriers, which causes water intrusion.

Ask plaintiffs about mold, and you get an entirely different story. They point to the modern day design and construction industry as the cause. The



advent of so-called "airtight" buildings that enhance energy conservation has contributed greatly to the problem, they say. Should moisture get into the interior of such a building, it can't get out.

Complicating the problem, lawyers say, are designers who specify building materials, such as paper-covered drywall and certain adhesives, that provide an excellent breeding ground for mold. Complex designs for many of today's high-style buildings can lead to radical roof, window and wall angles, increasing the chances of gaps and water intrusion. Inadequate or faulty HVAC systems are also pointed to as a cause of excess humidity. Finally, today's fast-track projects lead to faulty workmanship and insufficient time for materials to thoroughly dry before sealing them into an airtight environment.

## A Cause for Concern

Regardless of the cause, the fact is that mold now presents a significant liability concern and first party property problem for anyone involved with a building project or with an existing building, for that matter.

Currently, there are no exposure standards regarding mold and related toxins. In response to the recent spate of claims, however, some states are beginning to address this issue. California, for exam-

ple, recently passed the Toxic Mold Protection Act with directives to set indoor mold exposure limits and establish standards for detection and removal. We'll now have to wait and see how legislative bodies react to the current litigation trends and whether workable guidelines can be established.

A major concern for design and construction firms is that mold-related problems frequently involve construction defect claims that evolve into class-action lawsuits alleging personal injury due to long-term exposure to hidden mold. Often, statutes of limitation do not apply to these bodily injury claims. What's more, these bodily-injury claims can be accompanied by other claims from project owners and tenants for breach of contract, property damage, delays, business interruption and loss profits.

Should you be faced with these charges, will your insurance company be there to protect you? More and more, we are seeing mold exclusions added to homeowners' and general contractors' insurance policies. They are also starting to show up on policies written for building owners and tenants.

State departments of insurance have received hundreds of filings from insurance companies seeking to limit or exclude mold claims. Even where specific mold exclusions are not included in policy language, some insurers may try to exclude mold claims under existing pollution, contamination, seepage, or deterioration/wear-and-tear exclusions. Courts have ruled both for and against the denial of mold claims based on the standard pollution exclusion.

To date, we have yet to see a professional liability policy written for design professionals that includes a blanket mold exclusion. However, insurers are considering such exclusions and applying them to specific circumstances. If your professional liability policy is the only policy covering a problem building, the odds that the plaintiff's lawyer will file a claim against you dramatically increases.

## Recommended Actions

If you're in the construction industry, recognize that designing and building a mold-proof building is impossible. However, there are steps that you can take to help avoid extensive mold problems and thereby reduce the chances of expensive claims.

Following are some helpful loss prevention ideas:

1. **Educate the owner.** Discuss with your client the potential for mold problems and the need to design remedies into the structure rather than deal with the problem somewhere down the road. Point out that the owner will be liable for such problems should tenants, clients, customers or other third parties allege that they have suffered bodily injury due to mold.
2. **Know your locale.** Although the \$32 million dollar claim near Houston got the biggest headlines, mold is not a problem restricted to hot, humid climates like the Gulf Coast and the Southeastern United States. British Columbia, for example, recently faced a rash of million-dollar mold claims due to envelope failure and water intrusion involving poorly designed condominiums.  

You need to thoroughly investigate the history of mold problems in your locale. Check for any standards that may come into play in your state. If you are working on a project outside of your normal territory, consider peer reviews of your HVAC design and other humidity control measures by local consultants familiar with that environment.
3. **Design and build with mold in mind.** Don't skimp on mold-control measures, particularly in locales where it is a proven problem. Pay particular attention to HVAC and humidity-control systems. Ensure there is proper ventilation, including adequate crawl spaces, exhaust fans and dehumidifiers. Specify leak-proof window and door installations and mold-resistant materials. Ensure proper drainage and runoff controls so water doesn't collect underneath structures. Provide complete details for flashings. If the owner refuses your recommended mold-control items, document that fact in your contract or project files.
4. **Draft protective contract language.** A clear and accurate scope of services specifying who is responsible for mold is essential. Press for indemnity language that allocates liability for mold related claims to those in the best position to control the building environment. Avoid guarantees, warranties and other such language concerning the absence of mold.

**Mold** (Continued from page 3)

5. **Hold regular meetings during construction.** In your working agreement, call for regular inspection, testing and disclosure for existing mold as well as conditions that could lead to mold. When necessary, retain qualified industrial hygienists or other expert engineers to provide inspection and remediation services. Document all findings, changes in project scope, project upsets and other information that could be used in your defense of a subsequent claim.
6. **Provide maintenance guidelines.** Require that the contractor or manufacturer provide equipment maintenance programs for HVAC and other humidity-control systems. Call upon the building owner or manager to fix plumbing leaks and clean up and dry any water spills within 48 hours; keep HVAC units inspected and maintained according to manufacturer specifications, and provide proper venting of any installed moisture-generating appliances or machinery. Include in your recommendations an overall guideline to maintain low indoor humidity (generally below 60%).

For more guidelines, see the EPA's "*Mold Remediation in Schools and Commercial Buildings*," available at [www.epa.gov/iaq/molds/](http://www.epa.gov/iaq/molds/).

## Review Your Insurance Coverage

Almost all general contractors and sub contractors now have mold exclusions attached to their policies. Underwriters are reviewing this exposure carefully. One insurance company specifically excludes mold, and won't even consider providing coverage for a contractor that is in any way involved with mold.

At the same time, several insurance companies have developed specialized insurance programs for mold abatement. Once again, they underwrite the exposure very carefully paying particular attention to firm qualifications and experience.

If you are a building owner or tenant, evaluate your current coverage. Is mold specifically excluded? If so, is your exposure significant enough to be a concern? If so, is it possible to "buy back" the coverage by paying an extra premium to include coverage? If so, how much will it cost?

Mold is a major exposure for everyone associated with the building industry and buildings in general. As with any exposure, it can be reduced if appropriate steps are taken to identify the risk and then manage, reduce, and/or eliminate it, or transfer it to a third party (typically an insurance company).

We welcome any questions that you may have. 

***Disclaimer:** This article is written from an insurance perspective and is meant to be used for informational purposes only. It is not the intent of this article to provide legal advice, or advice for any specific fact, situation or circumstance. Contact legal counsel for specific advice.*

## Reduce Your Total Cost of Risk: Strategies for Winning

by James P. Schabarum II, CPCU, AFSB

Whatever the condition of the insurance marketplace, you as an insured can significantly reduce your "Total Cost of Risk" by implementing an effective Risk Reduction Plan™ (RRP) and developing relationships with your insurance partners. Having a well-developed RRP will result in long-term risk reduction and a favorable loss history. This will make your firm more attractive to insurance underwriters and enable you to obtain appropriate coverage at the lowest realistic price.

In order to make a cultural change from purchasing insurance to focusing on your total cost of risk, a comprehensive RRP will need to include:

1. **Relationship Audits** – Regular evaluations of your inside and outside teams' expertise, services and capabilities. In order to achieve excellent results, you need excellent players in key positions. Key positions include the company's risk manager or consultant, the safety manager, retail insurance

**Strategies** (Continued on page 5)

**Strategies** (Continued from page 4)

broker, excess and surplus lines broker or managing general agent, and underwriter.

**2. Industry-Specific Risk Surveys** – Continuous surveys should be performed to identify self-insured gaps in coverage, risk-related problems, and opportunities to reduce cost of risk. After analyzing the survey information, strategies should be developed and implemented to further reduce the cost of risk.

**3. Loss Control and Claims Management Protocols and Service Agreements** – Allocating resources to improve your loss control and claims management will have a significant affect on reducing your cost of risk. Simple measures, such as updating all your contractual, insurance and indemnity requirements to reduce or transfer risk, implementing tight first aid and return to work programs,

utilizing designated medical providers, pre-employment screening, and frequent review of open claims can result in substantial reduction of risk.

**4. Insurance Marketing** – A proactive, formalized, exhaustive marketing plan should be developed six months before your insurance renewal date. Consider alternative markets (captives, risk retention groups or capital market funds) along with assuming part of your risk through larger deductibles as well as tailored limits and coverages.

It's important to build strong relationships with your inside and outside teams. When possible, face-to-face meetings with your underwriter will allow you to focus on the hot key areas to improve your firm's attractiveness to specific markets. Having strong leadership and good communication among your team members will result in reducing your total cost of risk.✂

## Cavnignac Staff Shines This Summer!

Cavnignac & Associates employees will be busy this summer with the following events:

**Sue Marberry**, Office Manager, is a choir member of the First Unitarian Universalist Church of San Diego. On June 14th, the choir will perform a short Haydn mass and Durufle's Requiem as part of the Unitarian Universalist Church Concert Series. Sue will join the La Jolla Festival Chorus for the Summer Pops Concert on the pier on July 11th and 12th, performing the fourth movement of Beethoven's 9th and a number of other rousing choruses. Sue will also take part in summer sings with the Pacific Academy of Ecclesiastical Music (PACEM) at St. Paul's Cathedral in San Diego.

**Celia Mondfrans**, Account Manager in our Professional Liability Department, and her daughter belong to "Mothers and Daughters Club assisting Philanthropies" (MADCAPS). Although MADCAPS' main event is held in March (a show by 7th through 12th grade girls to raise money for their chosen philanthropies), over the summer the girls volunteer their time to do philanthropic work.

**Jeana Wallace**, Account Manager for our Employee Benefits Department, is a member of Junior League of San Diego. Since 1929, Junior League volunteers have partnered with the community to improve life in the San Diego area.

The Junior League sponsors such programs as the Education Toolbox (assists parents in finding the necessary resources to help their children succeed in school), Impact San Diego (addresses the urgent needs in the San Diego community immediate response), and the Storefront Shelter in Hillcrest (serves San Diego's teenage homeless population), to name a few.

**Ginger Cornwell**, Publications Coordinator, volunteers her time and talents to the Southern California Paint Horse Club, a non-profit organization that promotes the American Paint Horse. The Club's major Paint Horse Show of the year is the California Classic, which will be held at the Los Angeles Equestrian Center in Burbank, California on August 6th through 10th this year. See <http://www.socalpainthorse.com> for more information.✂

**Visit us**  
on the  
**Web!**



**[www.cavnignac.com](http://www.cavnignac.com)**