



## **CHINESE DRYWALL CREATES UNPRECEDENTED GROWTH AND RISK FOR RESTORERS**

*By David Dybdahl, CPCU, ARM, MBA December 7, 2009*

Chinese drywall remediation is shaping up to be the largest single source of potential new revenue for restoration contractors in history. According to the actuarial consulting firm Towers and Perrin the total economic losses from Chinese drywall as reported in the publication Business Insurance on November 2, 2009 could fall between \$15 billion and \$25 billion dollars. In relative terms this would exceed the loss costs of any one of the ten largest hurricanes in history including Katrina. It also represents 2/3 of the entire current annual revenue base of the fire and water damage restoration industry. Restoration contractors will face light competition for this work because remodeling contractors do not have and probably cannot get the appropriate liability insurance needed to perform this work and an asbestos remediation firm's overhead is too high to compete with the restorers. Restorers who plan for this new source of revenue can expand their operations with undue risk. However without risk management planning, contaminated drywall remediation will be high risk work that may be totally uninsured for the restorer.

Certified mold restoration contractors are ideally positioned in the market place to perform this remediation work because they have the equipment, trained personnel and customized environmental insurance packages that can all be adapted to perform this new scope of service. A traditional insurance program on any contractor will have significant coverage gaps for contaminated drywall work and should never be relied upon. Custom designed insurance packages for contaminated dry wall remediation work are available today at reasonable costs from ARMR.Network, LLC.

Restoration contractors face two distinct loss exposures related to Chinese drywall. First, drywall that was installed in routine fire and water restoration projects between 2004 and 2008 is a completed operations loss exposure which cannot be avoided by future actions. The second loss exposure is a contractor can decide to take on new jobs to remediate contaminated drywall which was previously installed by another contractor. In either case special modifications to the Commercial General Liability (CGL) and Contractors Pollution Liability (CPL) insurance policies of the restoration contractor will need to be made in order to be properly insured. This work should never be done without CPL coverage.

If a contractor purchased high quality insurance for mold work between 2004 and 2008, and maintains it, they could be covered today for claims that may arise from Chinese drywall. However a move at any time to more restrictive insurance coverage may retroactively eliminate coverage for previously insured operations. For this reason restoration firms should never change insurance companies without a comparison of the coverage offerings by a qualified specialist. Basing insurance buying decisions solely on the premium, limits and deductibles is very dangerous because none of the insurance policies sold are standardized and only a handful are specifically designed for a restoration contractor. Firms that either purchased CPL insurance in the past with coverage defects for Chinese Drywall loss exposures or never had CPL coverage may be able to purchase a CPL policy today with back dated coverage to fill the historical CPL coverage gaps plus will provide good quality coverage going forward. This backdated insurance is available today in most states through American Safety Insurance Company. To evaluate the need for backdated CPL insurance it is highly recommended that the past CPL policies purchased by the firm be reviewed by an ARMR.Network insurance consultant.

Chinese drywall liabilities will affect thousands of individuals and companies as the unfortunate owners of contaminated properties search for sources of funds to pay for the remediation of their property. Loss exposures can be traced to "responsible parties" including developers, construction managers, general contractors, subcontractors, building products suppliers, distributors and manufacturers. Literally tens of thousands of properties and responsible parties are affected. A series of exclusions and limitations in all standard property and liability insurance policies make it very unlikely that any of the parties associated with a property that has Chinese drywall installed in it will have any insurance coverage for the costs to remediate the property or pay for the injuries to the occupants. One exception to this general rule is fire and water restoration contractors who have maintained top quality insurance for mold losses, should also have coverage for Chinese drywall related losses from ongoing or completed operations. However most of the low cost liability insurance options offered to restoration contractors today will have significant coverage defects for Chinese drywall associated claims. ARMR.Net's highly qualified risk consultants help our clients evaluate their current and historical insurance coverage and create insurance packages to fill the coverage gaps if they do exist. For assistance in evaluating these complex insurance matters please contact one of our consultants for a no obligation review of your insurance program.

### **The Risks Associated With Chinese Drywall**

In short, some but not all sources of Chinese drywall off-gas sulfur dioxide gas which combines with water vapor to form airborne sulfuric acid within the built environment. Most contaminated drywall was installed in homes between 2004 and

2007 in at least twenty four and as many as forty one states. Restoration contractors may have installed contaminated drywall in their normal fire and water damage restoration work because Chinese drywall made its way into the general US inventory of drywall. The jury is literally out on the possible adverse health effects to the occupants of the contaminated buildings; these health affects at low concentrations do not appear to be acute. Buildings containing sulfur contaminated drywall, which can smell like rotten eggs or burned match's will need to be remediated. Remediation involves removing the drywall, assessing and correcting potential structural damage, and correcting the corrosion of electrical systems, and HVAC equipment. The average remediation cost of a contaminated building is estimated to be 60% of it construction cost. There are currently no accepted remediation protocols or standards for contaminated drywall. Damages from the drywall include remediation costs, damages to building contents, decrease in property value and stigma in resale, increased fire risk and adverse health effects to the occupants and to remediators.

**Traditional Insurance Coverage For Chinese Drywall Related Losses**

Chinese drywall claims encompass traditional construction defect insurance coverage issues and then superimpose various "pollution" exclusion implications. Construction defect claims introduce a series of complex insurance coverage issues in both property and liability insurance policies. In general, acidic gas will fall within the definition of a "pollutant" in both property and liability insurance policies because it is an "irritant" or "contaminant". Therefore losses associated with Chinese drywall will be impacted by pollution exclusions in virtually all forms of commercial insurance.

Commercial and Homeowners property insurance policies fundamentally insure losses from discrete fortuitous loss events which result from accidents and natural disasters. It is usually difficult to obtain coverage for a construction defect on a property insurance policy because the prerequisite "insured cause of loss" (fire, windstorm, lightning, ect.) is missing to trigger coverage under the policy. Commercial property insurance policies also have pollution exclusions. Therefore property insurance policies can be expected to deny a Chinese drywall loss because of the absence of an insured cause of loss and the effect of the pollution exclusion. As a result most property owners and their lenders will be left uninsured under property insurance policies for the costs to remediate Chinese drywall; bad debt is another risk for the remediators.

CGL policies require an "Accident" to trigger the coverage under the policy. Construction defect claims are routinely denied by insurance companies over the absence of a covered accident. Also exclusions in CGL insurance policies for damages to "Your Work" and "Impaired Property" can stand in the way of liability coverage for contractors who installed contaminated drywall. These same exclusions appearing on a CPL policy also can bar coverage for Chinese drywall related losses. However not all CPL policies have these potentially onerous exclusions. Good quality CGL and CPL policies can be purchased at reasonable premiums for this remediation work.

**Environmental Insurance Solutions**

To be insured for Chinese Drywall losses contractors need a properly structured CPL policy which does not have a Property Damage To Your Work or an Impaired Property exclusion in addition to a properly rated CGL policy. About 2/3 of the CPL policies sold to restoration contractors today contain these onerous exclusions. These same exclusions can be problematic in a mold loss so if a contractor has good quality coverage for mold they probably have good coverage for Chinese drywall. If new work to remediate contaminated drywall is undertaken it is very important to amend the insurance program of the contractor. This new scope of work falls outside the scope of covered operations in most restoration contractors insurance policies. Also if the CGL policy has the contractor rated as a janitor or a carpet cleaner and the firm is actually ripping and tearing out Chinese dry wall, the insurance company can at their discretion deny a drywall remediation claim or refuse to renew the policy based on a material change in the risk. We have insurance solutions available for this work with American Safety Insurance Company including coverage for prior acts and completed work.

**For assistance or information please contact: ARMR.Network, LLC. Home Office 877-735-0800**

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**About Us**

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