

An hourglass-shaped graphic with a globe in the top bulb and another globe in the bottom bulb. The top bulb is dark blue, and the bottom bulb is light blue. The hourglass is light gray. The globe in the top bulb is dark blue, and the globe in the bottom bulb is light blue. The hourglass is centered on the page.

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Toxic Mold: Insurance and Legal Issues

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Toxic Mold: Insurance and Legal Issues

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Summary

Allegations of bodily injuries and property damage resulting from toxic mold in home and work environments have triggered litigation across the nation, and, as a result, have prompted insurers and governments to grapple with coverage of risks to property and health resulting from exposure to mold. To minimize their financial exposure to these losses, insurance companies have variously been excluding mold risks from coverage on their standard policy forms, raising premiums, increasing deductibles, and capping coverage. The perils associated with toxic mold coupled with the insurance industry's reduction in coverage have attracted the attention of state and federal legislators. Many states now regulate coverage against mold-related damage. In Congress, H.R. 5040, alternatively entitled the "United States Toxic Mold Safety and Protection Act of 2002" and the "Melina Bill," would, among other things, establish a federal insurance program to cover risks related to toxic mold. Emphasizing insurance issues, this report provides a brief summary of perceived perils, legal issues, and legislation associated with toxic mold. As circumstances warrant, this report will be updated.

Overview. Fungi are ubiquitous; they are present in any indoor or outdoor environment. "Mold" is a general term referring to the collective products of several species of fungus. Allegations of bodily injuries and property damage resulting from toxic mold in homes and work environments have triggered litigation across the nation, and have prompted insurers to limit their coverage of risks to property and health resulting from exposure to mold.

The states and Congress are responding. States are examining the feasibility of mold exposure limits, assessment and remediation guidelines, and public education programs. For instance, California has passed legislation to force insurers to offer mold coverage, and to mandate that homeowners disclose mold problems when selling a house. Toxic mold has attracted congressional attention, too, prompting the introduction of H.R. 5040, alternatively entitled the "United States Toxic Mold Safety and Protection Act of 2002" and the "Melina Bill." H.R. 5040 would, among other things, establish a federal insurance program to cover risks related to toxic mold.

Risks to Health and Property. Mold can cause health problems and property damage. First, while the most common molds are harmless to humans, mold can cause a variety of ailments. Some molds can produce allergic reactions, and others, which are far less common, but are hardly rare, can produce toxic effects and infections. Symptoms associated with allergic reactions to mold include aggravation of asthma, a runny nose, congestion, cough, and eye irritation.¹ Molds that release mycotoxins in the air, such as the *Stachybotrys chartarum* strain, must reach toxic levels before illness occurs, but when they do, they can cause fatigue, headaches, nausea, asthma, and the inability to concentrate.² In the most serious, but scientifically uncertain cases, toxic molds allegedly can cause immune system disorders, chronic fatigue, organ damage, memory loss, and bleeding in the lungs.³

Second, mold can cause property damage. Residential and work environments provide three conditions for mold to thrive: (1) warmth (40° to 100° F); (2) moisture, often resulting from leaky roofs, defective plumbing, drainage problems, flooding, and even high-humidity; and (3) nutrition, such as certain types of insulation, wood, and carpeting.⁴ Modern energy-efficient buildings provide a conducive environment for mold growth: Sealed construction techniques can result in insufficient flows of fresh air and reduced evaporation of moisture, creating warm, moist breeding grounds. Older buildings also are not immune from mold contamination, particularly in areas subject to flooding, heavy storms, or high humidity. Remediation costs vary with the scope of mold growth in these structures.⁵ Inspection costs alone can range from the low thousands to millions of dollars.⁶ In the most extreme cases, the buildings cannot be repaired, but must be stripped to their foundations and rebuilt at a price exceeding the original building costs.⁷

Mold and the Courts. Some commentators claim that toxic mold is “the next asbestos.” Under diverse causes of action, such as negligence, strict liability, misrepresentation, breach of contract, and even mental anguish, plaintiffs have secured large judgments against diverse defendants, such as construction contractors, property

¹ For a general treatment of allergic reactions associated with mold, see “Mold Allergy,” a National Institutes of Health publication at:

[<http://www.niaid.nih.gov/publications/allergens/mold.htm>] visited July 9, 2002.

² For information on *Stachybotrys chartarum* and other toxic molds, see the Center for Disease Control website at:

[<http://www.cdc.gov/nceh/airpollution/mold/stachy.htm>] visited July 9, 2002.

³ See the Center for Disease Control website at:

[<http://www.cdc.gov/nceh/airpollution/mold/default.htm>] visited July 9, 2002.

⁴ For a general treatment of residential mold hazards, see “A Brief Guide to Mold, Moisture, and Your Home,” an Environmental Protection Agency publication, at:

[<http://www.epa.gov/iaq/molds/moldguide.html>] visited July 9, 2002.

⁵ For a general treatment of mold remediation see “Mold Remediation in Schools and Commercial Buildings,” an Environmental Protection Agency publication, at:

[<http://www.epa.gov/iaq/molds/images/moldremediation.pdf>] visited July 9, 2002.

⁶ See ENGINEERING NEWS RECORD, *Containing Noxious Mold* (May 3, 1999).

⁷ See TIME.COM, *Beware: Toxic Mold* (June 24, 2001) at:

[<http://www.time.com/time/health/article/0,8599,165155,00.html>] visited July 9, 2002.

managers, architects, school districts, real estate agents, and employers.⁸ This litigation is expensive and complex, often requiring medical experts, toxicologists, and other scientific experts to investigate and interpret evidence during discovery, and to establish and rebut complex issues regarding causation or harm during trial. Potential damages for these claims include medical expenses, repair and replacement costs, containment and remediation expenses, abatement and mitigation expenses, relocation expenses, diminution of value claims, and emotional distress.

Insurance Coverage. Whether standard insurance policies cover losses and liabilities caused by toxic mold is a significant concern for all affected by mold-related lawsuits. At the same time, insurance companies have increasingly sought to limit their coverage.

Two cases illustrate the sort of lawsuits insurance companies have faced with respect to mold-related damage. In 1999, Texas homeowners sued their insurer seeking \$100 million for mold damage, alleging that the insurer's delay in paying a claim for a plumbing leak allowed time for mold to grow, thrive, and reach toxic levels.⁹ The mold caused the plaintiffs to become ill and forced them to evacuate their house. In a case involving a claim for breach of contract, a Texas appellate court found that an insurance policy covered mold-related damage notwithstanding a mold-fungal policy exclusion in the disputed insurance contract.¹⁰ The mold growth occurred as a result of a leaking roof, a peril covered under the policy terms, and therefore the exclusion clause did not apply. However, had the mold been caused by peril excluded from the policy terms – e.g., negligent or faulty construction – then the exclusion clause would have applied.

Rattled by losses stemming from lawsuits and claims, and alerted to the potentially large risks posed by mold-related perils, insurance companies have sought to minimize their exposure to mold-risks. They have excluded mold risks from coverage on their standard policy forms, raised premiums, increased deductibles, and capped coverage. In fact, mold-risks may prove to be uninsurable or too expensive for the average consumer to afford. A number of factors suggest the uninsurability of, or the high costs associated with, mold risks: the global potential for mold-related claims, the number of people affected, the magnitude of the harm, the vast array of policies potentially affected (e.g., property, health, and liability), and the costs associated with investigating claims and defending lawsuits.

Government Responds. As insurers reevaluate the terms under which they will enter (or stay in) the mold-risk insurance market, the states and Congress are exploring legislative and regulatory responses to this problem.

The States. States are responding in diverse ways. Some are examining the feasibility of mold exposure limits, assessment and remediation guidelines, and public

⁸ See General Cologne Re for a representative list of the diverse range of lawsuits alleging damages caused by toxic mold at: <http://www.gcr.com/FACTWORLD.nsf/Doc/Toxmold2> visited July 3, 2002.

⁹ See *Ballard v. Fire Insurance Exchange*, summarized at: <http://www.gcr.com/FACTWORLD.nsf/Doc/Toxmold2> visited July 22, 2002.

¹⁰ See *The Home Insurance Company v. McClain*, 2000 Tex. App. LEXIS 969 (2000).

education programs. Some are allowing insurers to exclude mold-risks entirely. For instance, last year, insurance companies paid \$1.2 billion in mold-related claims in Texas alone. In the same year the Texas Department of Insurance allowed insurance carriers to phase out mold-coverage for all new homeowner policies. This year, a new insurance product offering “enhanced water coverage,” sells back the excluded protection at an average annual premium of \$2,000.¹¹ In addition to Texas, thirty-five states, either by legislation or regulation, have approved some form of mold exclusions – e.g., Louisiana eliminated all mold coverage, while North Carolina put a \$5,000 cap on mold-related payouts.¹² California has passed a “Toxic Mold Protection Act,” which forces insurers to offer mold insurance and requires a seller of property to disclose to a buyer when the seller “has knowledge of, or reasonable cause to believe in,” the presence of mold at health-endangering levels.¹³ Other states, such as New York and Michigan, are proposing similar mold disclosure legislation,¹⁴ while Maryland and New Jersey have passed bills to study health risks associated with mold.¹⁵

Congress. Mold risks have attracted Congressional attention, prompting the introduction of the H.R. 5040, alternatively entitled the “United States Toxic Mold Safety and Protection Act of 2002” and the “Melina Bill.” Among other things, H.R. 5040 would require the Director of the Federal Emergency Management Agency (FEMA) to establish and carry out a national insurance fund to cover risks resulting from toxic mold hazards in real properties. The program would be designed and administered with the goal of allowing individuals to acquire mold insurance at reasonable rates. The Director would be the architect of the program, although the extent of federal involvement in administering the program is uncertain.

More particularly, H.R. 5040 would require the Director to determine the types, classes, and locations of eligible properties; set the terms and scope of coverage (e.g., exclusions, liability caps, and deductibles); establish premium rates; and provide insurers a “reasonable” rate of return for their assistance with or participation in the program. The Director would be required to give priority to residential properties designed for the occupancy of one to four families when making coverage available under the program. If the Director, after conducting investigations and studies, determines that it would be appropriate to extend coverage to other types of properties, the Director could make insurance available to any types and classes of (1) other residential properties; (2) church properties, and business properties which are owned or leased and operated by small business concerns; (3) other business properties; (4) properties occupied by private nonprofit organizations; and (5) properties owned by State and local governments.

¹¹ See Dan Michalski, *Mold Can Be an Insurance Mess for Homeowners*, THE NEW YORK TIMES C-9 (June 16, 2002)(“Under the new policies, Texas homeowners can expect insurers to pay for the actual removal of mold and the replacement of rotted walls, floors, and furniture, but not for testing or the expense of living in a hotel while work is done.” Id.).

¹² See id.

¹³ The law will not be enforceable until the California Department of Health Services develops permissible exposure limits for molds, which must be finalized by July 1, 2003.

¹⁴ See *Florida May be Next Hotbed for Mold Legislation*, BUSINESS WIRE (July 23, 2002).

¹⁵ See Michalski, *supra*, note 11.

To the maximum extent practicable, the Director would be required to encourage private insurers to participate in risk sharing, financial, and other aspects of the program. The program would be implemented through private industry with the federal government providing financial assistance, unless the Director determines that the program cannot be carried out through the private sector or could be “materially assisted” by the federal government. Upon such a determination, the program would be implemented primarily as a government program with industry providing administrative (and, perhaps, risk sharing) assistance.

In order to provide toxic mold insurance at the earliest possible time, the Director could develop and implement an interim program that must end by September 30, 2004.