

Are Mold Claims Covered Under A Homeowner's Policy?

By: Everett Lee Herndon, Jr.

The wording of an insurance policy varies from insurance company to insurance company and from state to state. The question of whether a particular policy covers mold contamination and remediation is a definite "*Maybe ... Maybe not.*" The policy must be read carefully and analyzed in light of the facts of the loss. There is no magic phrase or answer for coverage questions other than "*Maybe ... Maybe not.*"

The Insurance Services Office, Inc. (ISO) publishes "standard" or "model" policies that often form the basis of many policies issued by the various insurance companies. While some companies adopt the ISO policies almost verbatim, other companies may make extensive changes. These policies may then vary from state to state in their specific provisions in order to comply with state insurance department regulations, legislation and court decisions.

All policies are generally interpreted in light of insurance industry custom, practice and history unless there are specific policy wording, legislation or court rulings to the contrary. The industry standard for the general interpretation of policy provisions and how these provisions affect particular claims or losses is *The Fire, Casualty & Surety Bulletins (FC&S)*.⁽¹⁾

Given the variety of property policies available, let's take one policy, a typical homeowner's policy, and explore some of its provisions in order to understand some of the basic concepts involved in interpreting the policy with the aim of determining whether any mold coverage exists. The concepts are basic to understanding most insurance policies. In as far as similar terminology exists in other property policies or first party policies, the same interpretations and conclusions will generally follow.

The factor most significant to the insured in obtaining coverage is what is known in the industry as the *open perils* provision of the homeowner's policy. The factors most relied on by the insurance company to deny coverage are: (1) no direct physical loss, (2) no covered event, (3) the mold exclusion and (4) the pollution exclusion.

Open Perils Coverage

The most commonly used ISO homeowner policy is probably the HO 00 03 04 91, the HOMEOWNERS 3, SPECIAL FORM. This policy is generally referred to as the HO-3 and was put out by the ISO in 1991. The HO-3 provides coverage for Dwellings and Other Structures as follows:

We insure against risk of direct loss to property described in Coverages A and B only if that loss is a direct physical loss to property.(2)

Some insurance companies change the wording slightly but the concept is basically the same. For example, the Allstate Deluxe Plus Homeowners Policy, in California, provides that:

We will cover sudden and accidental direct physical loss to property described in Coverage A - Dwelling Protection and Coverage B - Other Structures Protection except as limited or excluded in this policy.(3)

The insuring agreements of these policies provide basically the same type of coverage, i.e., *Open Perils* coverage. The HO-3 and its variations are *Open Perils* policies, an evolution from the policies that previously provided *All Risk* coverage.

The FC&S states that:

Open perils coverage is defined by the exclusions that apply to coverage. It is the broadest form of coverage because loss that results from a cause that is not specifically excluded in the form is covered.(4)

The problem in determining whether mold is covered under the *open perils* homeowner's policy is in determining whether a particular exclusion applies. If the loss is not subject to one of the restrictions or exclusions in the policy, the loss, mold in this case, is covered. Since the homeowner has an *Open Perils* policy the homeowner is entitled to expect the loss to be covered unless the insurance company proves the loss is subject to a restriction or exclusion. The insured has a duty to report the loss. Once the insured reports the loss and damage to the insurance company, the burden of proof shifts to the insurance company to either pay the loss or prove that the loss and damage are excluded. To deny the claim and withhold benefits, the insurance company must demonstrate that the loss is excluded.

Direct Physical Loss

Coverage for most homeowner's policies is couched in terms of "direct physical loss" to the insured property, as opposed to non-physical loss, e.g., a financial loss of value due to the economy or re-zoning. Some companies argue that if there is no traditional physical damage (e.g., fire, windstorm) there is no loss. Their argument is that the mere presence of toxic mold does not constitute physical damage. However, the term in the policy is "direct physical loss." For example, loss under the policy would include theft, wherein the object may be "gone" but without any proof of physical damage to the object. The stolen object is a "loss" even if undamaged. Mold and mycotoxins which render a building uninhabitable also constitute a physical loss to the insured.

In a case involving an *all risk* policy the court held that when the insured was forced to evacuate his building because of the threat of imminent collapse, the loss was covered.(5)

Another case with an *all risk* policy involved the accumulation of gasoline vapors within a church building such that the building could not be used while the condition persisted. The court held that this was direct physical loss, opening the door to a loss of use claim.(6)

Although water and mold normally do cause observable physical damage, it is not necessary for the mold to do so in order to trigger coverage. The uninhabitability of the property due to the presence of mold and mycotoxins constitutes a loss to the insured. If the loss is covered (see below), the insurance company has to repair the damage (remediation) and return the dwelling to its previous state of habitability, as it would after a fire. This normally means an expensive mold remediation project.

Covered Event

With an *open perils* policy, a "direct physical loss to property" is covered unless excluded. Mold will grow only if certain conditions (mold spore, water, time, food source and a bearable temperature) are present. The condition that is of interest in the insurance policy is water. Most policies contain a number of exclusions pertaining to water, e.g., flood, seepage and surface water. Nevertheless, there are many covered losses involving water and each covered water damage claim involves the potential for mold growth and contamination. Each water damage claim will have to be considered individually to determine coverage.

What constitutes a covered event or loss is dependent on the wording of the policy, specifically the exclusions and any exceptions to the exclusions. Take the case of a roof leak and a worn out roof. The HO-3 policy covers "against risk of direct loss to property." While the HO-3 excludes coverage for the worn out roof itself ("wear and tear" is excluded), the resultant water damage, and mold if it results, is covered. The HO-3 policy does not contain a provision excluding the water damage in a case like this. If water damage from the roof leak is not excluded under the HO-3, neither is the mold that is a consequence of the water damage. Other variations of the homeowner's policy may exclude the resultant water and mold damage. But, in the HO-3, while the leaking roof itself is not covered (wear and tear), the ensuing mold damage and remediation are covered.(7)

In a Texas case involving a new roof that leaked, with resultant water damage and mold, the insurance company claimed that the mold and construction defect exclusions applied. The court held that the mold was an ensuing loss (an exception to an exclusion) and thus was covered.(8)

The Mold Exclusion

When insurance companies analyze coverage and deny mold claims one of the most frequently cited exclusions is the one that specifically cites mold. The ISO, HO-3 provides that:

We do not insure, however, for loss:

2. Caused by:

e. (1) Wear and tear, marring, deterioration

...

(3) Smog, rust or other corrosion, mold, wet or dry rot:

...

(5) Discharge, dispersal, seepage, migration, release or escape of pollutants unless the discharge, dispersal, seepage, migration, release or escape is itself caused by a Peril Insured Against under Coverage C of this policy.

The Allstate policy provides that:

In addition, we do not cover loss consisting of or caused by any of the following:

15. (a) wear and tear, aging, marring, scratching, deterioration, inherent vice, or latent defect;

...

(d) rust or other corrosion, mold, wet or dry rot;

(e) contamination, including, but not limited to the presence of toxic, noxious or hazardous gasses, chemicals, liquids, solids or other substances at the residence premises;(9)

Even though both policies mention mold in the exclusion, it has to be remembered that the words of the policy must be considered in context. Under the concept of *ejusdem generis* (things of the same kind, class or nature), mold, as used in these exclusions, is to be viewed as the other words are, namely losses that occur naturally over a period of time. For mold to be excluded, it must fit into the category of the exclusions typically referred to as the "wear and tear" type exclusions.

In discussing these "wear and tear" type exclusions, the *FC&S* states:

These exclusions, applicable only to open perils homeowners coverage, are derived from the older all risk policy language and are intended to rule out coverage for two kinds of losses. The first are the nonfortuitous events - types of loss that are certain to happen over a period of time and therefore do not represent a risk of loss . . . In the second group are losses that are so controllable with reasonable care that only gross disregard by the insured will lead to loss . . . (10)

The *all risk* policy language that the *FC&S* is referencing is the recent all risk property policy which was derived from the old marine *all risk* insurance policies. *Open perils* coverage is rooted in marine all risk insurance traditions.

If the mold has occurred naturally over a period of time as a result of climatic or atmospheric conditions, such as high humidity, and is not the result of a covered event, the exclusion is applicable and properly cited. However, most mold claims encountered under property policies are as a result of some type of water damage, whether (1) sudden and accidental or (2) as a result of slow seepage and leakage, which may or may not be covered, depending on the policy language and the facts. Only a thorough investigation of the facts and a close reading of the policy will enable one to determine which category the loss falls

into.

If the mold developed as the result of a covered peril, that is, one not excluded under the *open perils* policy, then the mold is covered as a resulting damage just as the water damage is covered.

Prior to 1991, a previously undetected loss (mold, wet rot, etc.) caused by repeated seepage and leakage of a plumbing system was covered in as much as discovery of the problem by the insured constituted a new and unexpected loss for the insured. The 1991 ISO policy was written with an exclusion for mold, wet and dry rot. However, confusion arose since the 1991 policy still required the insured to protect the property from further damage once the loss was discovered, implying that the loss was covered, as it had previously been covered. The new ISO 2000 HO-3 policy seeks to eliminate this confusion and specifically gives back the coverage for an undetected loss of this nature. The intent of the HO-3 *open perils* policy was originally to only exclude coverage for further damage where no action was taken once a loss was discovered. The ISO 2000 policy makes the intent clear and removes the confusion and the debate that has existed for the past decade.⁽¹¹⁾ Not all insurance companies will adopt the new ISO 2000 provisions. The applicable policy must be read carefully for each loss.

Pollution or Contamination

Another frequently cited exclusion refers to pollution or contamination.

The *FC&S* traces the present pollution exclusion in the homeowner's policy to its derivation from the contamination exclusion in the early *all risk* marine insurance forms. The marine policies grouped the expected contamination by sea water with several other non fortuitous events, such as wear and tear. These clauses carried over from *all risk* marine policies to *open peril* homeowner's policies.

HO-3 policy exclusion 2(e)(5), "Discharge, dispersal, seepage, migration, release or escape of pollutants...", probably would not be applicable to indoor mold since mold would generally grow on the premises as the result of the presence of water. Mold would not normally be brought onto the premises and "discharged" onto the premises.

Even if the insurance company relies on the "discharge" requirement, many courts limit the "pollutants" to the traditional environmental pollutants, which would not include indoor mold.

Allstate policy exclusion 15(e), "Contamination, including, but not limited to the presence of toxic, noxious or hazardous gasses, chemicals, liquids, solids or other substances..." also has to be read in the context of the history of the pollution exclusion and with the placement of the exclusion within the Allstate homeowner's policy.

In specifically listing out such items as "...toxic, noxious or hazardous gasses, chemicals, liquids, solids or other substances...", Allstate, and other policies with similar wording, may be precluded by the principle of *ejusdem generis* from including such organic substances as mold within the exclusion. The items listed in the exclusion all appear to designate traditional inorganic environmental substances, and not organic organisms like mold.

The FC&S, in discussing the homeowner pollution and contamination exclusion(s), in the context of the placement of the exclusions within the policy states:

Given the context of the exclusion, it seems clear that the intent was to exclude from open perils coverage . . . events that did not depend upon accidental happening, but instead would occur, given time and the proper circumstances: physical property will wear out; it will become mildewed or rotten if subject to enough humidity over time; . . . (C)ontamination contains within it a sense of a process of deterioration, not loss from an immediate, abrupt event.(12)

Traditionally, if there is a covered event, such as the sudden and accidental pipe break or wind damage to the roof, all damages causally flowing from the covered event are covered. If the water is not cleaned up and the property is not dried out in a timely fashion and mold develops, as it may within 24 to 48 hours, the mold is a covered damage and must be remediated. The proximate cause of the mold was the pipe break or the wind damage to the roof.

Some insurance companies do argue that the mere presence of mold and /or mycotoxins constitute (1) contamination or (2) pollution or (3) toxic gasses, thereby triggering the pertinent exclusions. However, as related to the pertinent policy exclusions, it is not so much the mere presence of the mold and /or mycotoxins that is significant in an analysis of insurance coverage and loss as is the determination of the cause or peril. Damages flowing causally from a covered event are covered. When the proximate cause of a loss is a covered peril, such as wind/rain damage, broken pipe, etc., the subsequent damage is covered - including the causally arising mold.

Conclusion

Coverage determination in a mold loss is not subject to an easy answer. The specific facts of the loss and the wording of the policy will control. Each case has to be reviewed carefully with a very close reading of the policy. The only answer available today to the question of whether mold is covered under a homeowner's policy is "Maybe ... Maybe not."

1. This multiple volume publication is available from the National Underwriter Co. in either print or CD and is updated monthly. *The Fire, Casualty & Surety Bulletins*, The National Underwriter Company, PO Box 14367, Cincinnati, OH 45250-0367
(<http://www.nuco.com/>)

2. Insurance Services Office, Inc., HOMEOWNERS 3, SPECIAL FORM, HO 00 03 04 91, Section I - Perils Insured Against
3. Allstate Deluxe Plus Homeowners Policy, Section I - Your Property, Losses We Cover Under Coverages A and B
4. The *FC&S* Bulletins/PERSONAL LINES/Homeowners/Dwellings/Homeowners Exclusions
5. Hampton Foods Inc. v. Aetna Casualty & Surety Co. 787 f. 2nd 349 (1986)
6. Western Fire Insurance Co. v. First Presbyterian Church 165 Colo. 34, 37 P. 2nd 52 (1968)
7. Property Loss Adjusting, Volume I, James J. Markam, Editor, Insurance Institute of America, p. 55.
8. Home Insurance Co. v. Dennis D. and Claudia T. McCain, No. 05-97-01479, Texas App., 5th Dist.
9. Allstate Deluxe Plus Homeowners Policy, Section I - Your Property, Losses We Do Not Cover Under Coverages A and B, Exclusion 15
10. The *FC&S* Bulletins/PERSONAL LINES/Homeowners/Dwellings/Homeowners Exclusions/Open Perils Exclusions
11. The *FC&S* Bulletins/PERSONAL LINES/Homeowners/Dwellings/Homeowners Exclusions/Open Perils Exclusions
12. The *FC&S* Bulletins/PERSONAL LINES/Homeowners/Dwellings/Homeowners Pollution Exclusions/Evolution of the Homeowners Pollution Exclusion

Everette Lee Herndon, Jr., is a claims consultant and expert witness working primarily in insurance bad faith cases. Mr. Herndon was an adjuster for over 25 years. He is based in Rancho Murieta, Calif

E-mail: herndon@ranchomurieta.org

Presented at the Mealey's Mold Conference, Marina Del Rey, CA, June 25/26, 2001