



CORROSIVE DRYWALL CLAIMS

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Agenda Munich RE

- Where the claims are coming from
- Third Party Liability Claims
- First party Property claims
- Defendants/Policyholders involved
- Damages
 - Property Damage
 - Bodily Injury
- Claims handling issues
- Reserving considerations


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Where the claims are coming from Munich RE

- States where claims have been reported**
 - Florida 59%
 - Louisiana 21%
 - Mississippi 6%
 - Alabama 5%
 - Virginia 4%
 - Other States 5%
- Heat and humidity is needed for chemical reaction to occur. This should limit areas where future claims develop. There is evidence of corrosive drywall shipped to the west coast. The dry and moderate climate should minimize claims in western states.

** Consumer Products Safety Commission report 3/31/10


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Third Party Liability Claims

- Residential structures including single family homes, condominiums, and town homes
 - Up to 50,000 homes affected, 30,000 estimated in Florida alone.
 - Claims have been reported to insurance carriers in various forms and forums:
 - Individual homeowner claims both litigated and non-litigated.
 - Multiple homeowner litigation filed in state courts.
 - Class action consolidated in Louisiana Federal Court.
 - Over 3000 homes in Payton case alone
 - The Court has consolidated all cases for purposes of investigation, testing, and discovery.


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Third Party Liability Claims

- Commercial Buildings
 - Limited exposure due to type (thickness) of drywall used in commercial construction.
 - Corrosive drywall imported from China 1/2" thick.
 - 5/8" thickness or greater utilized in commercial construction
 - Claims reported where 1/2" thickness was utilized in tenant build out and improvements on commercial structures.
- Claims also reported on drywall not manufactured in China. Initial indications of no merit to these claims. Still requires costly investigation and testing.

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Defendants/Policyholders involved in drywall claims

- Homebuilders/Developers/General Contractors
 - Many builders remediating damages to homes regardless of insurance carrier participation.
 - Homebuyer warranty policies may provide coverage if claims tendered during warranty period.
 - Homebuilders that fund settlements faced with pursuing their insurance carriers, suppliers and subcontractors for recovery.
 - **Builders Mutual v. Dragas Management Corp.**
Virginia court recently ruled home builder violated voluntary payments provision in CGL policy. Carrier not obligated to reimburse home builder for \$5m paid to remediate homes.
 - Dragas has filed an appeal

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Defendants/Policyholders Munich RE

- Suppliers/Distributors
 - Anyone in the chain of commerce may be held strictly liable for all damages.
- Subcontractors/ installers
 - Drywall installer most common subcontractor implicated.
- Design Professionals (Architects, Engineers)
 - Minimal exposure given design professional limited role in construction process of residential structures.
- "Ancillary" parties
 - Plaintiffs' attorneys faced with the possibility of Chinese manufacturer and German distributor not funding settlement naming every party involved in the supply, distribution and construction of damaged components. Costs to defend these parties force carriers to look at economical considerations regardless of liability.

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First Party Property claims Munich RE

- Residential - Majority of claims. Due to differences in the type of drywall used in residential and commercial construction.
 - Many carriers disclaiming coverage
 - Damage to faulty, defective, inadequate products such as defective construction materials excluded under standard homeowner policies.
 - Pollution exclusion
 - **Finger v. Audubon Insurance Co.** - Louisiana District Court ruled that the pollution and contamination exclusion, gradual or sudden loss exclusion (which includes rust and corrosion), and the faulty, inadequate or defective planning exclusion **did not** apply to preclude an insurance claim for damage.
 - Audubon has filed an appeal.

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Property Damages Munich RE

- Cost of removing and replacing drywall.
- Damage to plumbing, HVAC systems, wiring, appliances, carpeting, flooring, appliances, etc.
- Loss of use/temporary housing.
- Reduction in property values.
- Expert Investigative and testing costs.
- Defense and coverage counsel costs.
- Litigation and expert costs anticipated to be 30%-50% of total damages.

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Property Damages Munich RE

- Consumer Products Safety Commission and HUD recommends complete removal/replacement of all components including drywall, wiring, plumbing, HVAC, appliances, flooring, fixtures etc.
 - Per CPSC this is the only way to insure all corrosive materials removed from structure.
 - \$50,000-\$150,000 average cost per home
 - Varies by size of home, amount of corrosive drywall installed and how widespread contamination is.
 - 641 single family homes in Western Florida repaired by Lennar Homes at average cost of \$94,000 including relocation of homeowners during remediation.
 - 72 condominium units in Virginia repaired by builder with average cost of \$70,000 per unit.

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Property Damages Munich RE


- Southeast Louisiana Federal Court awarded \$2.6m in damages to 7 families, including up to \$100,000 per family for loss of use.
- The court recently awarded \$164,049 to one family.
- Recommended complete "gutting" and replacement of home's interior.
 - Did not specify which party would fund settlement, and did not include any bodily injury damages.
 - These awards have "raised the bar" on potential claim value.

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Bodily Injury Damages Munich RE

- Headaches, respiratory problems, burning eyes, fatigue.
- EPA, CDC, Florida Department of Health have not concluded causal connection between claimed injuries and corrosive drywall.
- Symptoms dissipate/disappear when persons removed from affected structures.
- Experts caution too early to determine if any permanent long-term bodily injury.
- Upcoming trials will determine causal link, compensability.


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Claims Handling Issues

- Where will coverage issues be litigated - state or federal courts?
- Which policy periods are implicated?
- Is there an occurrence, if so, how many occurrences?
- How are coverage exclusions being applied, including business risk, and pollution exclusions?
- Are payments builders making covered damages or voluntary payments?
- Are all conditions to coverage satisfied (notice, cooperation)?
- Carriers need to take a "measured" approach on coverage.


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Reserving Considerations

- Number/type of structures
- Role of policyholder
- Number of policies triggered
- Primary v. excess/umbrella policies
- Policy provisions/exclusions
- Venue
- Risk transfer

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Number /type of structures

- If supplier/distributor- amount of corrosive drywall sold or shipped can be used to determine how many homes potentially involved.
- Type of structure - condos v. detached homes.
- Size of home
 - The larger the structure, the more drywall and damaged components affected.
 - Majority of claims involve standard tract homes and condos less than 2500 square feet.
 - Claims reported involving custom homes. These homes usually require additional engineering, and different size of drywall.

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Role of Policy Holder Munich RE

- All parties involved in the chain of commerce will be implicated and have potential exposure to these claims
- Home builder may be forced to fund settlement and pursue sub contractors, suppliers and distributors.
- Suppliers, distributors, subcontractors/installer
- "Ancillary" parties
 - Plumbing, electrical, HVAC, flooring, framing contractors, appliance and fixture suppliers.

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Number of policies triggered Munich RE

Majority of homes were built from 2005-2007 with damages discovered as late as 2009. Should limit the years of potential coverage to 2005-2009.

- There have been some isolated reports of corrosive drywall utilized in homes as early as 1999.

Coverage trigger

- In states that follow a manifestation trigger of coverage, (Louisiana) the policy period of first manifestation is the policy usually triggered. If multiple homes built span multiple years, then potential for multiple policies to be triggered.

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Number of policies triggered Munich RE

- In those states that have a continuous or injury in fact trigger of coverage, all policies from the date the homes were built potentially triggered.
- Policy language modifying trigger
 - Known loss/prior work/progressive damages/anti-stacking.
 - Policies written post-1990's normally contain language quantifying the definition of occurrence and number of policies at risk.
 - Standard CGL policies contain known loss language in insuring agreement, which limits the damage to the policy period of first knowledge by the insured.

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Primary v. Excess and Umbrella Policies Munich RE

- Expenses may represent up to 50% of the total dollars paid.
- Primary policies will bear the burden of expense costs, as excess policies will not drop down until all underlying primary policies have exhausted.
- Those primary policies funding the defense of class action or multi-party litigation will find it difficult to tender their limits.
- Allocation of Loss
 - Horizontal v. Vertical exhaustion varies by jurisdiction.

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Additional considerations Munich RE

- Policy provisions
 - Pollution exclusion
 - Business risk- work product, your work, etc.
- Number of occurrences.
- Deductible/SIR
- Venue
- Risk transfer language in construction and purchase contracts.
- Unknown if Chinese manufacturer or German distributor will contribute towards settlement, though Knauf has accepted service of class action lawsuit.

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Chinese drywall not the next asbestos Munich RE

- "Chinese drywall claims will likely be a manageable earning event for insurers. We don't expect Chinese drywall to be the next asbestos because of the following:
 - Imported drywall seems to be limited to a defined time frame.
 - Incident reports have been very geographically concentrated.
 - Tests are now being performed and evaluated to determine health implications.

In contrast, the use of asbestos was widespread, had been used in manufacturing for a significant length of time, and tests on health effects did not begin until decades after exposure had already been accounted."

*Moody's investors service report, March, 2010

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