

Dryvit® EIFS and the Changing Construction Marketplace:

Writing profitable construction liability policies that includes EIFS has never been easier with Dryvit

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Construction liability insurance for home builders and related construction professionals has been a contentious issue for insurance companies and their underwriters for more than a decade. A marked increase in litigation activity in moisture intrusion, construction defect and alleged hazardous mold (sick building) cases over the past decade have had a chilling affect on the willingness of many insurance companies to write construction liability policies. This litigation threat, combined with the lingering impact of unanticipated catastrophic losses in other liability business lines (9/11 claims, Gulf area hurricane claims, lower than expected return on investments, etc.), has created a void in insurance availability for many home builders, sub-contractors, and aligned construction professionals.

This unfavorable insurance climate has applied to all common residential cladding types over the past several years. While insurance companies, generally, have been reluctant to write construction liability policies no matter which cladding system

the builder and his or her subcontractors are using on the home, this paper deals specifically with the insurability of Exterior Insulation and Finish Systems (EIFS) in the residential building segment.

Among all cladding types, EIFS has been most directly targeted by insurance companies on the basis of unusually large amounts of litigation activity that took place between approximately 1995 and 2002, involving homes constructed in 1997 or earlier. In addition to a large number of individual law suits involving builders, contractors and EIFS manufacturers, there was also a significant class action product defect litigation movement, resulting in one major class action being certified. As a result, many insurance companies have implemented restrictions on EIFS in the writing of policies, or will not write them for contractors that install EIFS.

Given the changed construction industry dynamics that we will describe later in this paper, however, as well as an unwillingness to distinguish the differences that exist in the approach of various EIFS manufacturers to the issue, that position relative to EIFS as a whole amounts to a very significant lost business opportunity for insurance companies today.

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What has changed?

Almost everything. In addition to environmental changes that will be described later, the fundamental underpinnings of the litigation environment is no longer applicable in the current EIFS construction marketplace.

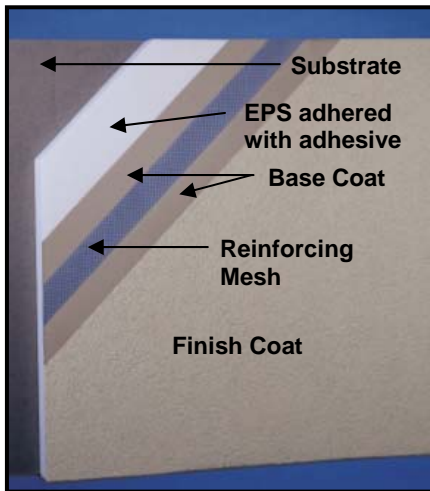


Diagram 1

With virtually no exceptions, all of the EIFS litigation activity that has taken place in the past has been based on allegations of design on the use of so-called barrier EIF systems in residential construction. Available under various trade names, barrier EIF systems are recognizable by the fact that the system is usually applied (adhered) directly to the building substrate, usually plywood or oriented strand board (OSB). **(See diagram 1 at left)** While barrier systems have been used successfully on tens of thousands of homes around the country since 1969 in the United States – and since the late 1940's in war-torn Europe – the simple reality is that building code requirements changed in the year 2000 to require components not previously required in the barrier EIF systems. As a result, barrier systems of any type, EIFS and non-EIFS, are no longer code-approved options in residential construction under the revised International Residential Code (IRC) – the governing, universal code body for residential construction.

The Development of Drainable EIFS Technology

Out of the code change requiring a secondary weather-resistive barrier to protect the substrate and a positive means of drainage was born the new class of residential drainage EIFS. These new EIF systems are, from the studs out, the same as cavity wall systems sometimes found in brick, wood, vinyl and other common residential cladding systems. They also feature, among other things, a secondary weather barrier often found with other common residential cladding systems. These new drainage systems (**see diagram 2 at left**) have completely changed the EIFS construction environment, making EIF systems better in how they handle moisture than any other common residential cladding system. It also should encourage insurance companies and their underwriters to re-evaluate their viewpoint on EIFS because the foundation of their concern relative to litigation and claims activity has been overwhelmingly changed. With drainage systems in place in the EIFS residential marketplace since the code change in 2000, the results – in terms of claims filed and loss history – show clearly the need to look at EIFS and their insurability in a new and very favorable light.

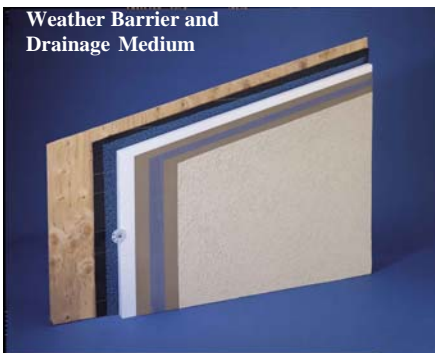


Diagram 2

Improved Construction Quality Emphasis

Another significant factor driving improvement in the residential marketplace has been industry-wide

**Explosive Growth
in EIFS “Doing It
Right” Trained
Contractors
Since 1998**

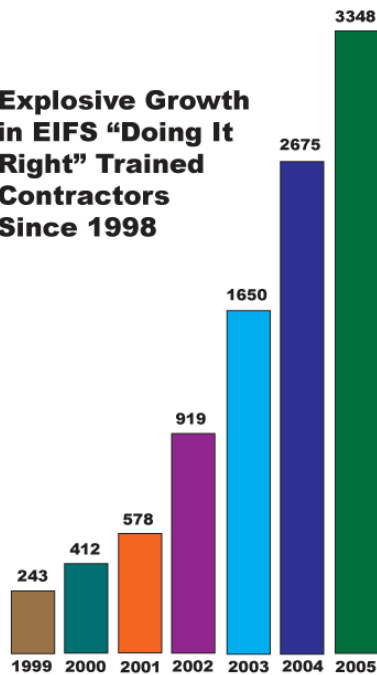


Diagram 3

emphasis on overall construction quality. In the EIFS contractor group, this emphasis is seen through efforts made by the Association of the Wall and Ceiling Industry (AWCI) and their innovative “Doing It Right” and *EIFSmart* contractor training programs. Since 1999, when just 243 contractors went through the program, the program has exploded. In 2005 more than 3,300 contractors earned their “Doing it Right” or *EIFSmart* certification, clearly demonstrating the growth of a highly-trained contractor base. (See Diagram 3 on left) The increased training emphasis has resulted in tangible gains in the AWCI-run contractor/applicator insurance program. In 2004, for example, AWCI collected \$2,414,100 in premiums on 145 policies, and paid out just \$3,000 in claims over that same year. The 2005 data, while still being finalized, was performing even better over the first 9 reported months of the year: \$2,192,638 in premiums on 225 policies and paid out just \$6,125 in claims. AWCI’s experience has demonstrated conclusively that the use of well-trained contractors can lead to low loss history and highly-profitable insurance policies.

Not All EIFS Are Created Equal

Industry training emphasis is not the only quality driver. Manufacturers like Dryvit Systems, Inc., for example, have quality programs of their own. Dryvit provides detailed product information training for listed contractor/applicators. Dryvit

also provides a video training module that provides applicators with a visual reference on proper application techniques, as well as web-based written application instructions, specifications and typical details for use by the construction and design community. In addition, Dryvit products are manufactured under the most rigorous standards for quality and consistency in the EIFS industry. Dryvit is the only EIFS manufacturer to have all of its manufacturing facilities ISO 9001:2000 certified, meaning that Dryvit products are consistently of a high quality and help to ensure an optimal application on the wall.

As an indication of the company's confidence in the moisture drainage system and the importance of contractor training, Dryvit now offers a 30-year warranty when the builder is a member of NAHB and receives an application education from Dryvit, builds with the Residential MD[®] or Sprint MD[®] system, and uses a Dryvit trained and AWCI *EIFSmart* contractor on the job.



Loss and Claims History Data Shows Dramatic Trend

The results of all of these changing construction marketplace factors has been positive, at least as it pertains to Dryvit claims that have proceeded to litigation.

Since the new IRC code went into effect, the lawsuits filed have been in a dramatic decline. In fact, over the past eight years, Dryvit has averaged **less than one** lawsuit per year on its residential drainable EIFS, and has suffered **no** indemnity losses in those cases.

The Dryvit litigation data is interesting, too, in that the majority of the cases filed were limited to just three states, North and South Carolina and Alabama. Virginia and Oregon were next, with smaller case loads filed in Ohio, Illinois and Pennsylvania. Not only were the lawsuits limited to a few states, but also to a very small number of very active law firms, many of which actively sought out claimants for the cases. As those law firms have turned their attention to other potential product claims outside of the EIFS industry, it is clear that the litigation activity has dramatically diminished.

The factors that led insurance companies to restrict the writing of EIFS policies have either substantially changed or have been eliminated altogether.

Conclusions

The factors that led insurance companies to exclude EIFS from their policies have either substantially changed or have been eliminated altogether. Changes to the residential construction environment, enhanced contractor training and building codes have all led to much lower overall risk. With a dramatic reduction in claims and litigation activity already evident, the conditions exist for insurance companies to write profitable

policies that include EIFS if they carefully screen their builders, contractors, and manufacturers to ensure they are adhering to the highest quality and consistency standards available today.

Tighter underwriting standards – making sure that builders and contractors are using code compliant systems and products and are trained in the application of EIFS – are crucial. Understanding that not all EIFS are equal is another critical factor. Only the manufacturers who adhere to ISO manufacturing standards and commit to and support training initiatives should be considered for insurability. If underwriters demand the highest standards of quality in the industry, they will be able to profitably and confidently write policies that include EIFS in the years to come.