

# CHINESE DRYWALL SUMMARY AND UPDATE

**Between 2003 and 2007, the U.S. construction industry needed more drywall than domestic manufacturers could supply to meet the surging demand from new construction and post-hurricane reconstruction. During these boom years, an estimated 500 million pounds of drywall was imported from China - enough, according to estimates, to build 70,000 to 100,000 homes.**

Most of the imported drywall was used in residential construction. Alleged problems with the product emerged. We offer a summary of the problems, the investigations, the litigation, the public and political outcry and the insurance issues raised.

## THE PROBLEM

The imported drywall allegedly emits sulfur gases causing one or more of the following:

- A rotten egg-like odor
- Corrosion of certain metals, including copper, copper alloys and silver (piping, air conditioning coils, faucets, electrical outlets) near the drywall
- Health-related complaints, including allergic reactions, coughing, respiratory and sinus problems and throat infections

The economic impact is difficult to estimate. According to the National Association of Home Builders, the remediation cost per home could range from a third of the home value to \$100,000. Some sources estimate total economic losses in the \$15-\$25 billion range, including litigation expense, bodily injury and indirect costs (e.g., loss of use, diminution of home value). If these predictions are accurate, the losses will compare to those of some of the most damaging hurricanes in history.



## THE INVESTIGATION

- As of January 25, 2010, the Consumer Product Safety Commission (CPSC) had received 2833 drywall incident reports from 37 states, the District of Columbia and Puerto Rico. Over 90% of the reports were from five states: Florida (59%), Louisiana (21%), Mississippi (6%), Alabama (5%) and Virginia (4%). Environmental conditions, such as high humidity, high temperature and poor air circulation, have been identified as possible contributing factors. The CPSC estimates that 5,000 homes have registered complaints about drywall.



- The CPSC released a report in late 2009 which found “a strong association between the problem drywall, the hydrogen sulfide levels in homes with that drywall and corrosion in those homes.” This report was based on studies conducted of 51 homes located in Florida, Louisiana, Virginia, Alabama and Mississippi. This was the first governmental report linking corrosion problems with the Chinese drywall. The CPSC is still investigating the link between Chinese drywall and the health complaints. The report, along with other information, can be found on the **CPSC web site**.
- In late 2009, the CPSC announced that it was expanding its investigation to include American-made drywall, following reports of complaints from owners of homes built exclusively with American-made drywall. Lawsuits have been filed against two American drywall manufacturers.
- The Interagency Task Force on Chinese Drywall was established to coordinate the investigation and sharing of information among multiple federal agencies. The CPSC is leading the federal investigation along with other federal and state agencies, including the Centers for Disease Control (CDC), Environmental Protection Agency (EPA), Agency for Toxic Substances and Disease Registry (ATSDR) and the Department of Housing and Urban Development (HUD). Joining them are scientists, environmental consultants and forensic experts, each of whom will conduct their own investigations.
- **This is one of the largest investigations conducted in the history of the CPSC, which is dedicating 15% of its staff to the effort along with officials from other agencies and outside testing labs. In the last five months of 2009, CPSC spent over \$3.5 million in direct costs on the drywall investigation.**
- HUD and the CPSC recently issued **guidance** on identification of problem drywall in homes. However, studies for remediation protocols are continuing and results are not expected to be released until spring 2010. At present, no approved remediation protocols exist.

## THE LITIGATION

- With the exception of a few actions by homebuilders, all of the lawsuits, both state and federal, have been brought by homeowners seeking damages for property damage, personal injury and associated consequential damages. Class action lawsuits have been filed on behalf of thousands of homeowners primarily in Gulf Coast states.
- The defendants in these actions are various manufacturers, suppliers and builders. Two of the largest manufacturers, Knauf Plasterboard (Tianjin) Co., Ltd. and Taishan Gypsum Co., Ltd., are foreign corporations. Taishan Gypsum, a company reportedly controlled by the Chinese government, did not respond to the complaint filed against it and a default judgment was entered.
- In June 2009, multiple pending federal actions involving liability for Chinese drywall were consolidated in multidistrict litigation (MDL) which is pending in New Orleans. MDL is a federal court procedure for consolidating related federal cases pending in different jurisdictions. The purpose of the MDL is to streamline and expedite resolution of the mass litigation by identifying representative cases and issuing court decisions that will impact other pending litigation. Other related actions pending in federal districts will be treated as

tag-along actions. Additional details surrounding the pending MDL litigation can be found on the [U.S. District Court website](#).

- The early MDL trials are expected to focus on the extent of home remediation required, and to establish a benchmark for repair protocols and appropriate compensation for different types of damage. Plaintiffs argue that it is necessary to tear out all drywall, fixtures, wires and pipes and completely rebuild the interior. Defendants are expected to argue for less costly remediation efforts. The later stages of the litigation are expected to address some of the ancillary costs incurred by homeowners as well as the health-related complaints.
- The initial MDL test case, *Germano et al v. Taishan Gypsum Co. Ltd. et al*, involved seven Virginia plaintiffs whose homes have drywall manufactured by Taishan Gypsum Co. The plaintiffs seek \$2.5 million in damages. The trial, technically a default hearing, recently concluded and the decision is still pending.
- In January 2010, the Louisiana attorney general's office filed a lawsuit against manufacturers and home developers alleging loss of expected revenues as well as claiming costs related to remediation and disposal of contaminated drywall.
- The trustee for homebuilder WCI Communities has filed a lawsuit against 14 insurance companies seeking coverage for losses in connection with tainted Chinese drywall. The WCI Drywall Trust was formed under a bankruptcy plan to pursue insurance recoveries. More than 700 homeowners may seek recovery through the trust.

## POLITICAL/MEDIA ATTENTION

- The issue has received international political attention. Drywall was the subject of meetings between U.S. and Chinese government officials during President Obama's visit to China in late 2009. Reports suggest that the Chinese made no financial commitment, but they are fully cooperating with U.S. investigative efforts.
- A lead plaintiff in one of the pending class actions is Sean Payton, head coach of the Super Bowl Champion New Orleans Saints.

Many media reports have focused on stories of extreme family hardship. One New Orleans resident's home was destroyed by Hurricane Katrina before being rebuilt with allegedly tainted Chinese drywall. When his family started getting sick from the fumes, he moved out. His homeowner's insurance carrier denied the claim and subsequently non-renewed the coverage - because it was an unoccupied residence.

- Legislation and other initiatives designed to further investigate and provide relief to affected homeowners have been introduced at the federal, state and local levels.
- The plaintiffs' bar is fully engaged, supporting active websites and educational seminars.

## INSURANCE COVERAGE

While a number of lines of insurance may be implicated - Commercial General Liability (CGL), Property, Pollution, Environmental, Professional, Products and Excess Liability - CGL coverage is likely to be most heavily involved. CGL may provide the sole source of coverage for many entities. CGL carriers can be expected to push back based on applicable policy period (trigger), definition of terms such as occurrence, bodily injury and property damage (including rip and tear) and policy exclusions for "your work," "your product," "impaired property," "pollution," "recall of products" and "known injury or damage."

This list of potential coverage defenses is by no means exhaustive. Coverage will ultimately be determined by the terms and conditions of each policy and, importantly, the state law that applies. For example, application of identical pollution exclusions may yield different results depending on whether the policy is subject to Louisiana or Florida law.

Few, if any, carriers are undertaking defensive or investigative activities of drywall-related claims without fully reserving their rights to decline



coverage. Those entities that have procured Pollution coverage and/or Contractor's Rework coverage (rip and tear) are likely to be better protected.

## SUGGESTED ACTIONS

**If you are an installer, distributor, contractor or are involved with drywall in some other capacity, we suggest that you undertake, at a minimum, the following steps to be prepared in the event a claim is presented or suit is filed:**

- Attempt to trace the source of drywall used in your business over the last several years, especially for projects that occurred between 2003 and 2007.
- Review project specifications, along with company documentation of compliance with those specifications.
- Obtain and review terms of all related purchase orders, invoices, etc. to ascertain whether indemnity may run in your favor with regard to the drywall supplier/manufacturer.
- If you are an upstream contractor/developer, gather all contracts and certificates of insurance with respect to the installation of drywall and evaluate potential contractual risk transfer opportunities.
- Gather and review all potentially relevant insurance policies for each project and ensure timely notification should a claim be asserted.
- Engage claim advocacy professionals for both pre- and post-claim discussions to maximize claim outcomes and protect your interests.

For additional information you can read our June, 2009 issue of **Blueprint** on this same topic.

## CONTACTS

For more information, or if you have any questions, please contact:

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