

# Pollution Occurrence Insurance

*For weatherization assistance program providers, obtaining affordable coverage is unexpectedly difficult.*

by Robert C. Adams

**W**hat is pollution occurrence insurance (POI), and why do Weatherization Assistance program (WAP) providers need to be concerned with it? This is the question on the minds of many people working in and around the WAP at the state and local levels. And if it is not yet on your mind, it will be soon.

The need for POI is tied into the WAP's involvement with lead hazard control—another issue that would seem to be of little importance to a federally funded energy conservation program. After all, the WAP installs energy conservation materials and performs limited health and safety repairs. Lead-based paint hazard control programs, like those operated through HUD, are usually focused on prime window and door replacements, surface paint stabilization, kitchen and bathroom remodeling, and exterior wall covering replacements—areas of the home that the WAP rarely disturbs. Why should very limited WAP resources be used to perform very expensive services that conserve little energy?

The authorizing legislation for DOE's WAP (10CFR Part 440) does not mention lead-based paint hazard control. Indeed, DOE policy notices forbid the use of WAP funds to perform abatement, control, or stabilization work. However, these policies do require workers to conduct activities in a safe manner to avoid contaminating homes and to avoid exposing themselves and their families to this hazard. When WAP crews disturb surfaces that may contain lead-based paint, they must safeguard people through a prescribed set of work practices, referred to as lead-safe weatherization (LSW). The LSW protocols require crews to perform setup and cleanup routines to contain the lead dust and debris generated from the weatherization activities (see "Lead-Safe Weatherization," *HE* May/June '03, p. 24). The



improved safety features now included in the revised WAP protocols protect both the customer's and the worker's families from the harmful effects of lead-based paint dust. Every state has adopted these work standards, and nearly all crews and contractors have attended training in their state on performing lead-safe weatherization work.

In other words, the WAP is not involved in lead hazard control beyond ensuring that no lead-based dust or other contaminants are created as a result of the conservation work being performed in the home—a rather simple mandate. But here's the catch. HUD recommends that precautions must be taken regarding lead-based paint when using federal funds to work in homes that

- were constructed before 1978; and
- have not been determined to be lead-based paint free; and
- in which the amount of disturbed lead-based painted surface exceeds 2 ft<sup>2</sup> per room of interior surface, or 20 ft<sup>2</sup> of exterior surface, or 10% of a small component type such as windows; or

- the amount of lead-based paint dust that will be generated exceeds OSHA's defined airborne levels for lead.

These conditions apply in nearly 70% of the homes weatherized each year by the WAP.

Further, weatherization providers are required to either give or mail to occupants a copy of the EPA booklet *Protect Your Family from Lead in Your Home* at least seven days before work is to take place. Under the EPA regulations, local agencies who do not give and document proper notification could incur hefty fines if they are found doing weatherization work in pre-1978 homes where more than 2 ft<sup>2</sup> of paint surface is disturbed.

And finally, DOE has stated in their program notices that adequate liability coverage must exist to protect state and local agencies in the event of an incident that happens while crews are installing materials in the home. Their definition of adequate coverage includes contractor's liability insurance to protect against poor workmanship and liability insurance to

protect against incidental disturbances of environmental pollutants like lead-based paint dust—also known as POI.

### *Is Finding POI Coverage Difficult?*

Unfortunately, obtaining affordable POI coverage has proven to be more difficult than was originally expected. The difficulty is twofold. First, insurance claims in the residential market have skyrocketed in recent years. This is due in part to mold and mildew issues in both new and older housing, and in part to an increase in damages sustained as a result of weather-related disasters, such as Hurricane Floyd in 1999 and recent tornadoes, hail and ice storms, and flooding. Second, the number of insurance carriers willing to offer this coverage has declined dramatically over this same period. This decline was further complicated by the losses sustained by the insurance industry as a result of the September 11, 2001 terrorist attacks and the subsequent economic slowdown. Insurance companies lost money and moved quickly to eliminate any products deemed risky or unprofitable. Because POI coverage on a scale like the one being contemplated through the WAP was relatively new, it seemed likely that insurance companies would brand this coverage as a risky product.

Indeed, insurance difficulties cropped up repeatedly in the responses to a survey conducted in January 2002 by the National Association for State Community Services Programs (NASCS), the member organization representing the states in Washington, D.C., on matters related to the WAP and the Community Services Block Grant. Twenty-four states (46% of the DOE grantees) responded to this short survey, which was designed to uncover the states' progress, or the hurdles they faced, in obtaining POI coverage. The states that responded represented 539 local agencies, or 56% of the local WAP network. The survey found that

- 24% of respondents believed they had adequate pollution occurrence insurance;
- 76% of respondents had no POI coverage, couldn't find coverage in their area, or were unsure of their status; and

- Only five states (or 21%) believed their local network was in compliance with the DOE policies governing liability insurance coverage.

### *What Do I Need to Know About POI?*

Purchasing the right coverage to protect your organization or company is not an easy task. Liability insurance is a very serious issue, and purchasing the

increase. Also, if the deductible is increased, the premium may sometimes decrease—but not always. For example, consider a POI policy in which the deductible is \$2,500 and the premium payment is \$1,500 for about \$50,000 worth of work volume—what a small agency would perform. Doubling the deductible to \$5,000 does not decrease the premium; it will remain at \$1,500. Not a sound business move. It only makes sense to consider increasing the



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A weatherization crew member identifies duct leaks in a Maryland home. WAP agencies need adequate liability coverage to protect themselves in the event of an accident.

wrong policy could be catastrophic. If you have questions or concerns, you should consult a licensed insurance broker or your legal representative to make sure you are making sound decisions about your coverage and your risks. Here are a few tips that may help you to ask the right questions.

Every POI policy has three basic limits—per occurrence (the maximum amount to be paid for each recognized claim); aggregate (the maximum to be paid for all claims made during the policy term); and deductible (the initial amount paid by the insured when a claim is made). As a rule of thumb, when the occurrence and aggregate limits are increased, the premium will

deductible when an agency's premium is more than \$3,500—reflecting closer to \$1 million in volume. The premium could decrease by \$200 to \$300 if the \$2,500 deductible was doubled, a condition that a larger agency with greater assets might find more acceptable than would the smaller agency with the \$50,000 contract.

The cost of POI coverage will depend on the volume of work being performed by the local agency or contractor. A premium amount will be established when the policy is issued. Most policies include a minimum premium amount—an amount established by the carrier to underwrite the policy. Additional costs will be

incurred as the volume increases, but not proportionally. For example, at \$50,000 in volume, the minimum premium might be \$1,500. At \$100,000 in volume, the premium might be \$1,550 (the minimum premium of \$1,500 plus a fee of \$50 for increased volume). At \$500,000 in work volume, the premium might be \$1,750 (the minimum premium of \$1,500 plus a fee of \$250 for increased volume).

POI policies generally cover the work being performed in a specific project and will exclude unrelated activities. In other words, a POI policy for the WAP would cover any work performed under any WAP agreement but could exclude rehabilitation services paid for by HUD, local funds, or other sources.

The insurance industry offers a lead-based paint policy to contractors and organizations performing lead-based paint projects that are usually funded in whole or in part by HUD. Lead insurance is for those companies doing demolition or rehabilitation work where painted surface disturbance is unavoidable. Such situations could include remodeling kitchens and bathrooms, removing walls, and replacing siding and roofs. Personnel performing lead paint stabilization or abatement work must have lead technician, lead supervisor, and/or risk assessment training and certification. Of course, the premium cost for these policies is extremely high—\$10,000 to \$20,000. Since weatherization crews do not intend to identify or disturb surfaces that may contain lead-based paint, and since our crews are trained in lead-safe practices aimed at reducing or eliminating any lead dust distribution, weatherization crews can purchase POI policies at more affordable rates.

Most POI policies include an exemption for mold and mildew coverage. As of now, 38 states either allow insurance carriers to exempt mold and mildew from homeowners' policies or permit the carrier to severely limit the level of claim for mold or mildew incidents. A rider can sometimes be purchased to include mold and mildew on a POI policy; however, these riders

are very expensive—they can more than double the cost—and not all companies offer them.

Finally, for agencies, there is at least one alternative vehicle for acquiring liability coverage. Some agents offer riders to existing errors and omission (EO) policies (also known as director's liability policies) that protect an agency against unintentional mistakes in information. This type of insurance rider could protect an agency without purchasing a POI policy if agency staff performs such limited WAP services as auditing, building analysis, and quality control inspections, and if it uses private contractors to install weatherization materials. Of course, the private

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contractor would need either a POI policy or a rider to his or her general liability policy. A few companies already include environmental matters in their EO policies, but most require added coverage. Again, not all companies will add a rider to their EO, due to risk.

### ***Who Should Purchase POI?***

The answer to this question depends on the state. In order to comply with DOE requirements, states may opt to purchase, or arrange for the purchase, of single policies that cover the entire WAP project. Or the state may pass the responsibility for procuring POI coverage to the local agencies, who will purchase the POI coverage directly; or require their contractors to purchase the coverage; or do both—purchase coverage and require contractors to do the same. Confused?

Essentially, there is no best way to purchase POI coverage for the WAP. Each state and local agency will have to formulate a strategy that fits its individual circumstances and complies with its

legal team's advice. The following is a brief discussion of how these policies can be obtained within the various levels of the WAP network.

### **State Insurance Office**

Most states are self-insured and do not purchase insurance on a routine basis. A few states have, or will soon attempt to purchase, POI coverage for their network. For example, the Commonwealth of Virginia has purchased POI coverage for the state's network of WAP agencies. The states that would pursue this option have fully operational insurance offices or divisions

whose staff are familiar with the insurance industry and who are capable of negotiating terms and conditions for specific coverage. In these cases, the state insurance office staff conducts the industry analysis; performs a risk assessment to determine coverage requirements; offers a request for a proposal or an invitation for bid to the insurance industry; and

makes the purchase based on the offers received. Usually, the WAP enjoys a low premium cost, since the state purchases just one policy, rather than purchasing separate policies for each agency and/or contractor.

There are disadvantages to this procurement method. Generally, insurance carriers do not multiply coverage for each agency included as a named insured party in a blanket policy. The aggregate amounts available for the policy are shared by the group and can be diluted. If several claims are made in a year, the later claims could have little or no coverage, since limits were used on previous claims. Also, there are few companies in the country willing to underwrite multimillion dollar liability policies for thousands of residential properties that are unknown at the time of application. This limits the field of prospective bidders.

### **State Associations**

Several states (such as New York and Arkansas) are using or plan to use their

state community action or WAP association to act as the conduit for the purchase of a blanket POI policy for the group. In these cases, the association purchases the policy and becomes the insured party, or negotiates a reduced price schedule on behalf of the association members. Agencies either join the master policy as named insured or purchase individual policies from the recommended broker.

The cost of these policies is usually less than market rate because the purchase is negotiated. If the association negotiates a master agreement, the WAP pays a lower policy premium, because one policy is purchased rather than separate ones for each agency or contractor. If individual policies are negotiated, the cost is usually fixed below market rate because the carrier applies a volume discount.

There are drawbacks to procuring POI coverage through an association master agreement that are similar to those encountered under the state purchasing method that was described above. The most important of these is that the association could find itself in first position regarding liability issues. This means that, in the event of any legal action, the association would probably be named as a defendant, since it would be viewed as the entity with the deepest pockets when a claim was made. The association would be required to excuse itself from the lawsuit by proving that it had no role in causing any injury to the claimant. The association would have to work to clear these legal hurdles, even if it did not directly supervise the work that was the subject of the lawsuit.

### Local Agencies

Until a painted surface is disturbed, the mechanical systems are tested, or particles of dust are redistributed, no liability exists for the WAP. The actual need for POI coverage begins with the local agency, since the liability starts when work is initiated in the home. It is the providers of direct services that run the risk of disturbing any building component that contains lead-based paint.

As I explained above, most states are self-insured and do not normally

procure project insurance, especially liability coverage like POI. For this reason, most state WAP offices will pass the responsibility for purchasing POI coverage on to the local agency network through the contract or grant document. The POI insurance procurement issues will differ depending on which delivery model is used—direct hire, private contractor, or a combination of both.

**Direct hire.** In a direct hire, the agency employs staff who work directly

that of any group procurement. Any claims made against the policy will have a direct effect on future premiums, since there are no other group members to share the liability.

**Private contractor.** One of the trends over the last few years has been the increased use of private contractors to perform some or all of the WAP services in the home. The use of private contractors eliminates the need for a local agency to incur the expense of



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Sealing a bypass in this Illinois home requires some adroit maneuvering in a tight space.

for the WAP. These staff supervise the project; conduct building analyses and energy audits; install energy efficiency materials; conduct health and safety testing and remediation work; perform heating and cooling system tests and service; conduct quality control inspections; and satisfy all of the file documentation and reporting requirements. Under the direct-hire method of service delivery, the local agency will purchase a POI policy or a POI rider to its general liability policy using its broker.

The local agency does not have to share occurrence and aggregate limits, since a single policy is issued, and the costs can be easily tracked through the liability insurance budget line item. This will help the state to track the cost of insurance for planning in future years. Unfortunately, the cost of this individually negotiated policy will be higher than

employing and training staff, warehousing materials, purchasing and operating vehicles, purchasing and using equipment, and so on. It is important to note that these costs, including insurance costs like POI, are charged by the contractor to the agency through the material and labor expenses incurred on each job.

Some local agencies may be willing to accept the liability for their contractors and purchase the POI policy on their behalf. In these cases, the policy will name the local agency as the insured party and the private contractors will be added as named insured to the policy. The cost of the insurance is dramatically reduced, since only one minimum premium payment is paid. For this reason, some agencies in Kansas, Mississippi, and Louisiana are applying for coverage on behalf of

their contractors, although at press time the underwriter had not decided whether to accept the application and provide a binder.

But if an agency takes on this role, its exposure is dramatically increased. This could mean that any mistakes made by the contractor in the area of pollution control could become the responsibility of the local agency. The local agency could stand in first position regarding liability and could be included in any legal action. This could occur even though agency personnel performed no direct supervision of the work. Also, the limits of coverage are shared by all parties named in the policy. If several claims are made in a year, the later claims could have little or no coverage if limits were used on previous claims.

To address these concerns, many local agencies will pass all liability requirements on to their private contractors and create hold harmless agreements to protect the agency from any claims being made. Each contractor will be required to purchase a POI policy or rider. Because the policies are purchased individually, the cost is higher than it would be through a group purchase. This procurement method can prove very costly, especially when the local agency uses several contractors. For example, if five contractors purchase POI policies at a minimum of \$1,500 each, \$7,500 will be spent on insurance costs. If the local agency purchases a single policy at the aggregate volume level, the cost will probably be less than \$2,000.

**Combination of direct hire and contractor.** Many local agencies now supplement their direct-hire crews with private contractors for certain services within the WAP. The use of a combination delivery system by a local agency complicates the issue of procuring POI coverage. The local agency is required to maintain POI coverage, since in-house crews and staff perform some of the work that results in the disturbance of painted surfaces. This results in the purchase of at least one POI policy. However, each contractor who engages in similar work is required to maintain POI coverage as well. This means that these contractors will purchase POI

policies separately, and will charge the cost through the labor and material line item of their contract with the agency.

All the pros and cons related to the local agency procuring POI coverage also apply to this combination scenario. And, all the pros and cons related to using a private contractor will also apply, making this scenario the most complicated of all.

### *Does the WAP Really Need POI?*

Some members of the WAP network maintain that purchasing POI coverage is unnecessary. Their logic is that we do not need insurance if we do the work properly. In fact, this is true. Unfortunately, insurance is never purchased with the intention of using it. You don't buy car insurance so you can go out in the morning and cause an accident. You don't buy homeowner's insurance so you can flood the basement and pay for the damages. And you don't buy health insurance to cover an illness you are planning to have in the future.

You buy insurance so you have financial protection if during the course of daily events something happens that you didn't plan to happen—an automobile accident, a flooded basement, or an unexpected illness. If we knew that we could attain a perfect safety record in weatherizing every home, no agency or contractor would ever need workers' compensation, or contractor's liability insurance, or vehicle fleet insurance, or POI coverage. Unfortunately, life doesn't come with guarantees, and sometimes things happen that we didn't foresee. And so the WAP network will purchase POI coverage and continue to strive for perfection so we never have to use it.

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