

**REPORT OF THE
STATE CORPORATION COMMISSION'S
BUREAU OF INSURANCE ON**

**Insurance Coverage For Damage
To Foundations And Other
Home Structural Components**

**TO THE GOVERNOR AND
THE GENERAL ASSEMBLY OF VIRGINIA**



HOUSE DOCUMENT NO. 12

**COMMONWEALTH OF VIRGINIA
RICHMOND
1994**

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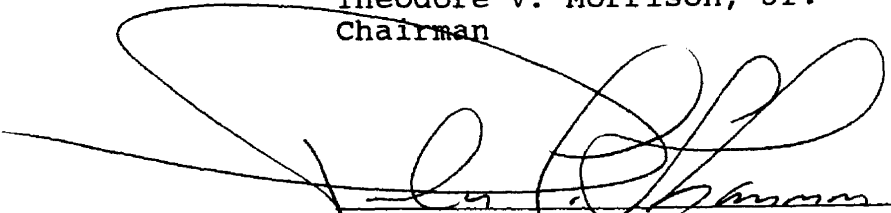
TO: The Honorable L. Douglas Wilder
Governor of Virginia
and
The General Assembly of Virginia

We are pleased to transmit this Report of the State Corporation Commission's Bureau of Insurance on Insurance Coverage for Damage to Foundations and Other Home Structural Components.

The study was initiated and the report prepared pursuant to House Joint Resolution No. 644 of the 1993 Session of the General Assembly of Virginia.

Respectfully submitted,


Theodore V. Morrison, Jr.
Chairman


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EXECUTIVE SUMMARY

Purpose of Study

House Joint Resolution No. 644 was passed by the 1993 General Assembly requesting the State Corporation Commission to conduct a full investigation and study of (i) insurer claims adjustment and settlement practices concerning foundation and other structural damage under homeowners insurance and home protection insurance contracts, and (ii) policy exclusions and other language in such insurance contracts relating to coverage for damage to foundations and other home structural components. This study was requested because many homeowners have suffered financial losses from structural damage to their homes as a result of shrink-swell soil conditions in Chesterfield County, and insurance policies often exclude or provide little coverage for this type of damage.

Findings

The State Corporation Commission's Bureau of Insurance (Bureau) conducted a survey of the top twenty-five writers of homeowners insurance in Virginia, all five home protection insurance companies licensed in Virginia, and three risk retention groups that write liability policies for builders in Virginia. The Bureau also conducted an investigation into the claims adjustment and settlement practices of three of the companies that were surveyed; an investigation was conducted on the one risk retention group chartered in Virginia and on the two home protection companies that indicated on the surveys that they provide coverage for structural damage. Several real estate firms were also contacted as well as the Richmond Association of Realtors and the Home Builders Association of Richmond. The findings contained in this report reflect data gathered as of October 1, 1993. The following summarizes the findings contained in this report.

1. Homeowners insurance policies are not required by statute to provide coverage for damage to foundations or other home structural components resulting from shrink-swell soils. Homeowners policies provide coverage for structural damage if such damage is caused by a peril the policy covers. Coverage for earth movement is generally excluded. Some companies allow their insureds to buy back certain coverages that are otherwise excluded under the policy. These coverages may be purchased for an additional premium. Of the twenty-five homeowners insurance companies surveyed, only one indicated that, for an additional premium, it will provide coverage for structural damage resulting from shrink-swell soils.
2. Home protection insurance companies are not required by statute to provide coverage for damage to foundations or other home structural components. One home protection company actively markets a product in Virginia that provides coverage for structural damage. Another home protection

company continues to provide such coverage for existing insureds but no longer actively markets policies providing coverage for structural damage to new customers. Two other home protection companies are licensed in Virginia but do not offer coverage for structural damage. An additional company has had its license suspended in Virginia and is no longer permitted to write new business.

3. Three risk retention groups write liability policies in Virginia for builders. These policies indemnify builders against their liability arising from non-performance under the warranties they give on new homes. Structural damage caused by shrink-swell soil conditions may be covered by such home warranties. Warranties are not regulated by the Bureau of Insurance because they are not insurance products. The extent to which risk retention groups are regulated by the Bureau depends on whether they are chartered in Virginia or outside of Virginia. The federal Liability Risk Retention Act of 1986 gives state insurance departments limited authority over the regulation of risk retention groups that are not chartered in their state. Only one of the three risk retention groups surveyed for this report is chartered in Virginia. Those chartered outside of Virginia do not have to seek approval by the Bureau for policies issued in Virginia. One of the risk retention groups chartered outside of Virginia has, with certain exceptions, been temporarily enjoined from issuing new policies in Virginia.
4. Title 38.2 of the Code of Virginia allows real estate agents and home builders to sell home protection insurance contracts without being licensed as insurance agents. None of the real estate firms contacted for this study sell home protection insurance contracts that provide coverage for structural damage. According to the Richmond Association of Realtors and the Home Builders Association of Richmond, home warranties provided by builders and the "back up" liability insurance policies for these warranties are generally not marketed through real estate agents but are marketed by the builders themselves. Some site agents may be marketing warranties on behalf of the builders they represent.
5. Transactions involving real property are governed under Title 55 of the Code of Virginia. Several legislative changes to this title have been enacted over the past two years. Effective July 1, 1993, §55-518 was amended to require the builder of a new dwelling to disclose in writing to the purchaser all known material defects which would constitute a violation of any applicable building code. Section 55-70.1, which pertains to implied warranties on new homes, was amended in 1992. Subsection B of this section requires a vendor, who is in the business of building or selling dwellings, to warrant to the vendee in every contract for the sale of a new dwelling, that the dwelling with all its fixtures is sufficiently (i) free from structural defects so as to pass without objection in the trade, (ii) constructed

in a workmanlike manner so as to pass without objection in the trade, and (iii) fit for habitation. The 1992 amendment extended the required one-year warranty to a period of five years for structural defects in the foundation of new dwellings. The term "structural defects," as used in this section, means a defect or defects which reduce the stability or safety of the structure below accepted standards or which restrict the normal use thereof.

6. An investigation of the two home protection companies that provide coverage for structural damage and the one risk retention group chartered in Virginia revealed that claims were generally handled in accordance with contract language. Specific instances of violations of the standards set forth in Virginia's unfair claims settlement practices laws will be addressed in market conduct examination reports issued by the Bureau.

Conclusion

Generally, coverage for damage to foundations and other home structural components resulting from shrink-swell soil conditions is excluded under homeowners insurance policies. In addition, coverage for this type of damage is provided in some home protection contracts but is excluded in others. The Bureau found that, generally, the three companies investigated for this study are paying claims in accordance with their policy provisions. Any instances of claims settlement practices which are not in compliance with policy provisions on file with the Bureau or which are not in compliance with the standards set forth in the unfair claims settlement practices laws of Title 38.2 of the Code of Virginia will be cited in the Bureau's market conduct reports.

GENERAL ASSEMBLY OF VIRGINIA--1993 SESSION

HOUSE JOINT RESOLUTION NO. 644

Requesting the Virginia State Corporation Commission to study the practices and contract of insurers issuing homeowners insurance policies and home protection insurance contracts concerning coverage of damage to residential foundations and other residential structural components.

Agreed to by the House of Delegates, February 7, 1993

Agreed to by the Senate, February 16, 1993

WHEREAS, shrink-swell soil conditions in portions of Chesterfield County have resulted in cracked foundations and other significant structural damages to several hundred residences; and

WHEREAS, consulting engineers estimate that necessary repairs to these damaged homes will cost over six million dollars; and

WHEREAS, as a consequence of insurance policy exclusions, policy interpretations denying coverage, and claims adjustment and settlement practices, or combinations thereof, insurers have refused coverage in many cases and provided little coverage in others; and

WHEREAS, such insurers' coverage exclusions and coverage denials have resulted in financial crises for many Chesterfield County homeowners left with repair bills averaging over \$15,000 per home at last estimate; now, therefore, be it

RESOLVED by the House of Delegates, the Senate concurring, That the Virginia State Corporation Commission (SCC) be requested to conduct a full investigation and study of (i) insurer claims adjustment and settlement practices concerning foundation and other structural damage under homeowners insurance as defined in § 38.2-130 of the Code of Virginia and home protection insurance contracts as described in Chapter 26 (§ 38.2-2600 et seq.) of Title 38.2 of the Code of Virginia, and (ii) policy exclusions and other language in such insurance and contracts as the same relate to covering damage to foundations and other home structural components.

The Virginia State Corporation Commission shall report its findings, conclusions, and recommendations to the Governor and the 1994 Session of the General Assembly as provided in the procedures of the Division of Legislative Automated Systems for the processing of legislative documents.

INTRODUCTION

Legislative Request

The State Corporation Commission was requested by the 1993 General Assembly, pursuant to House Joint Resolution No. 644, to conduct a full investigation and study of (i) insurer claims adjustment and settlement practices concerning foundation and other structural damage under homeowners insurance and home protection insurance contracts, and (ii) policy exclusions and other language in such insurance contracts relating to coverage for damage to foundations and other home structural components.

As stated in the resolution, this study was requested for the following reasons:

- (1) shrink-swell soil conditions in portions of Chesterfield County have resulted in cracked foundations and other significant structural damage to several hundred residences;
- (2) insurers have refused coverage in many cases and provided little coverage in others; and
- (3) insurance policy exclusions and claim denials have resulted in a financial crisis for many homeowners in Chesterfield County, leaving many homeowners with repair bills averaging \$15,000 per home.

Methodology

The State Corporation Commission's Bureau of Insurance (Bureau) began its research by conducting a survey of the top twenty-five writers of homeowners insurance policies in Virginia. Based on figures reported in 1993, these insurers accounted for over eighty percent of the premiums written in Virginia for this line of insurance during the previous year. A list of the insurers surveyed and their 1992 written premiums is included as Appendix I in this report.

A survey was also sent to all home protection insurance companies licensed in Virginia. A total of five home protection companies are licensed in Virginia, and all five are domiciled in the Commonwealth. (See Appendix II for a chart showing these companies' 1992 written premiums.) Four of these companies are licensed and in good standing. This means they are in compliance with the financial requirements of Virginia insurance laws and are permitted to write new business. These four companies are American Home Shield of Virginia, Inc., HAA of Virginia, Inc., Mid-Atlantic Insurance Corporation, and United One Home Protection Corporation of Virginia. The other company, Realsafe Corporation of Virginia, Inc., had its license suspended in April of 1992 and is prohibited from writing new business.

Another survey was sent to three risk retention groups which provide "back up" insurance for home warranties sold in Virginia.

One of these, HOW Insurance Company, A Risk Retention Group, is chartered in Virginia, and as such, is licensed as a liability insurer and is subject to the same laws applicable to all other liability insurers licensed in Virginia. National Home Insurance Company (A Risk Retention Group), which is chartered outside of Virginia, has been issued a temporary injunction and, with certain exceptions, is prohibited from writing new business in Virginia as of June 30, 1993. Western Pacific Mutual Insurance Company, A Risk Retention Group, was also surveyed. This risk retention group is also chartered outside the Commonwealth of Virginia. A chart showing these risk retention groups' 1992 written premiums is included as Appendix III.

The purpose of each of these surveys was to determine:

- (1) whether any companies provide coverage for damage to foundations and/or other home structural components resulting from shrink-swell soil conditions;
- (2) whether any companies provide coverage for damage to foundations and/or other home structural components resulting from something other than shrink-swell soil conditions;
- (3) the number of claims reported to the companies for damage to foundations and/or other home structural components in Virginia between January 1, 1990 and December 31, 1992;
- (4) the number of claims paid, the total dollar amount paid, the number of claims still pending, the number of claims denied, and the reasons given for the denials; and
- (5) whether the claims data compiled by the companies could be broken down to show (i) the number of claims for damage to foundations and/or other home structural components resulting from shrink-swell soil conditions, as compared to (ii) the number of claims for damage to foundations and/or other home structural components resulting from something other than shrink-swell soil conditions.

In addition to sending the surveys, the Bureau conducted an investigation of the two home protection companies that had indicated on the surveys that their contract provides coverage for structural damage. The Bureau also conducted an investigation of the one risk retention group chartered in Virginia. The purpose of the investigations was to review the companies' claims settlement and adjustment practices.

Finally, the Richmond Association of Realtors was contacted as were ten real estate firms which represent a large portion of the residential real estate transactions in the Richmond area. These firms were contacted to determine what information is given to home buyers or potential home buyers regarding the protection afforded by home warranties and home protection companies.

BACKGROUND

Shrink-Swell Soil

Although the information collected for this study was not limited to any one area of the state, the impetus for the study, as noted in House Joint Resolution No. 644, was the shrink-swell soil problems faced by many homeowners in Chesterfield County. Shrink-swell soils, or expansive soils, are soils that have a high clay content and are subject to extreme fluctuations due to moisture content. They decrease in volume, or shrink, when they become dry and increase in volume, or swell, when wet. As they increase and decrease in volume, they can exert several thousand pounds of pressure per square foot on foundations. Foundation problems can occur when the moisture levels change in the soil below the footings or along basement walls.¹

Soils with significant shrink-swell potential are found in many areas throughout the United States. The situation is not unique to Chesterfield County. In fact, shrink-swell soils may be found in every county in Virginia. The problems encountered in Chesterfield County have been due in part to a combination of expansive soil conditions, construction practices, and extended drought periods.²

Initiatives Taken by Chesterfield County

Chesterfield County has undertaken several initiatives aimed at resolving many of the problems attributable to shrink-swell soil. In January, 1992, the Board of Supervisors established a Commission on Soils and Foundations to look into measures that could be taken to assist homeowners with shrink-swell soil damage. The Board of Supervisors also increased the number of inspectors in the Building Inspection Office to allow for more thorough inspections of home construction in the future.³

In November, 1992, a Shrink-Swell Soil Task Force was established to assist the county in drafting two policies. One policy established a revised minimum standard footing requirement for residential foundations; the other called for on-site inspectors from private engineering firms or the county's Building Inspection Office to inspect all residential footing pours as well as on-site concrete testing. The task force set up an automated complaint tracking system and was also responsible for developing a special training program for all inspectors within the Building Inspection Office. Provisions were also made in the department's budget to provide for an on-going training program.⁴

In order to provide assistance to homeowners who had already experienced damage from shrink-swell soil conditions, a program titled the Citizen Assistance Program was set up to (i) retain several engineers to review homes where shrink-swell soil was evidenced and (ii) retain the services of several legal firms to provide consultation to citizens whose homes had sustained damage

from shrink-swell soil conditions. An ombudsman was hired to coordinate and administer this program. In addition to these efforts, the county has prepared several brochures which provide information to homeowners on how to reduce the risk of damage due to shrink-swell soils.⁵

Protection for Shrink-Swell Soil Damage

Despite the efforts taken by Chesterfield County, the financial problems faced by many county residents have not been eliminated. These problems have been compounded by the fact that insurance policies do not necessarily provide protection for damage caused by shrink-swell soils. In fact, most homeowners policies do not provide coverage for damage to foundations and/or other home structural components resulting from shrink-swell soil, nor are they required to do so by Virginia insurance law.

Home protection insurance contracts do not necessarily provide coverage for structural damage nor are they required to do so by Virginia insurance law. A home protection insurance contract is defined in §38.2-2600 of the Code of Virginia as any contract or agreement whereby a person undertakes for a specified period of time and for a predetermined fee to furnish, arrange for, or indemnify for service, repair, or replacement of any and all of the structural components, parts, appliances, or systems of any covered residential dwelling caused by wear and tear, deterioration, inherent defect, or by the failure of any inspection to detect the likelihood of failure. The term "structural component" is defined in §38.2-2600 as the roof, foundation, basement, walls, ceilings, or floors of a home.

Structural damage caused by shrink-swell soil conditions may be covered by home warranties which are provided by builders to cover defects in the homes they build. Certain implied warranties are granted to new home buyers by statute. Title 55 of the Code of Virginia sets forth standards for implied warranties on new homes. Home warranties are not regulated by the Bureau of Insurance because they are not considered insurance contracts. In fact, any warranty provided by a manufacturer or seller of goods or services is not considered insurance and is not regulated by the Bureau of Insurance.

Home warranties may be backed by a liability insurance policy which provides coverage directly to the builder to indemnify the builder against liability arising from non-performance under the builder's warranty. The builder is the insured under this type of policy. This differs from coverage provided under a home protection insurance contract where the home buyer is the insured. Policies which provide this protection vary from company to company.

An explanation of the way insurance products and warranties are regulated in Virginia is included in subsequent sections of this report.

Special Insurance Program Sought for County Residents

Early in 1993, the DeJarnette & Paul Insurance Agency contacted RLI Insurance Company about developing a policy to insure the residents of Chesterfield County against damage due to shrink-swell soils. A questionnaire was mailed to all of the residents in two of the county's subdivisions to determine the level of interest in such a policy. In order to justify the start-up costs, the company needed a positive response of at least 300 residents before it could consider developing a special program to insure this type of risk. Since only 121 responses were received, the program was never implemented.

REGULATION OF INSURANCE PRODUCTS

The State Corporation Commission's Bureau of Insurance regulates the business of insurance transacted in Virginia. This authority extends over the lines of insurance being studied in this report, i.e. homeowners insurance, home protection insurance, and liability insurance. This authority does not extend to warranties provided by manufacturers or sellers of products or services, including home warranties provided by builders. The extent of the Bureau's authority to regulate risk retention groups varies according to whether the risk retention group is chartered in Virginia or outside of Virginia. This authority is based on the federal Liability Risk Retention Act of 1986.

The following information describes how the Bureau regulates the policy forms, rates, unfair trade practices, and unfair claims practices of companies writing homeowners insurance, home protection insurance, and liability insurance in Virginia as well as risk retention groups conducting business in Virginia.

Regulation of Policy Forms

The State Corporation Commission is given the statutory authority in Title 38.2 of the Code of Virginia to regulate homeowners insurance contracts, home protection insurance contracts, and liability insurance contracts delivered or issued for delivery in Virginia. These contracts must be approved by the Bureau of Insurance before they may be used.

In addition to the statutory authority granted in Title 38.2 of the Code of Virginia, the Bureau also has rules governing minimum standards for homeowners insurance policies. These rules are established in Regulation No. 17, and all homeowners policies delivered or issued for delivery in Virginia must at least meet these minimum standards. These standards do not require homeowners insurance companies to provide coverage for damage to foundations or other home structural components due to shrink-swell soil conditions. If such coverage were required to be provided, the rates charged for homeowners policies would have to contemplate this coverage.

The Bureau is also responsible for approving liability insurance policies issued by risk retention groups chartered in Virginia. These must be approved before they are used. Liability insurance policies issued by risk retention groups chartered outside of Virginia, however, are not subject to the Bureau's approval. The Bureau does have the authority, however, to prohibit any policy provision that is prohibited generally by state statute or declared unlawful by the highest court of the state. This is provided for in the federal Liability Risk Retention Act of 1986. Virginia's laws governing risk retention groups are set forth in Chapter 51 of Title 38.2 of the Code of Virginia. There are no provisions in this chapter requiring risk retention groups to provide indemnification against liability

arising from damage to foundations or other home structural components due to shrink-swell soil conditions.

Home protection contracts issued in Virginia must adhere to certain standards as provided for in Chapter 26 of Title 38.2. The provisions of Chapter 26 apply to all companies licensed as home protection companies in Virginia. Some provisions of the chapter also apply to property and casualty insurance companies that are permitted to transact home protection insurance as defined in §38.2-129. These provisions include §38.2-2606 and §§38.2-2608 through 38.2-2614. Section 38.2-2608 sets forth requirements for home protection contracts such as being written in simple and readable words with common meanings so as to be understandable without special insurance knowledge or training. Section 38.2-2608 also stipulates that every application or agreement must state that the purchase of the contract is not mandatory and may be waived.

Home protection contracts may or may not provide coverage for structural damage. These contracts may agree to indemnify for service, repair, or replace structural components, parts, appliances, or systems of a residential dwelling.

Rate Regulation

Rates for homeowners policies are subject to the "file and use" rating laws found in Chapter 19 of Title 38.2. These rates must be filed with the Bureau before they may be used. Rates for most liability policies are also subject to the file and use provisions of Chapter 19.

Home protection companies must file their rates with the Bureau in accordance with the provisions of Chapter 20 and must have the rates approved before they may be used.

Rates charged by risk retention groups chartered in Virginia are regulated in the same manner as rates for liability insurance policies. However, rates charged by risk retention groups not chartered in Virginia do not have to be filed or approved prior to being used.

Regulation Over Unfair Trade and Claims Practices

Companies that write homeowners insurance, home protection insurance, and liability insurance in Virginia are subject to the provisions of the Unfair Trade Practices Act set forth in Chapter 5 of Title 38.2. In general, these provisions prohibit false and deceptive advertising as well as unfair claims settlement practices. The Bureau has also issued Regulation No. 12 which further establishes minimum standards for claims settlement practices.

Risk retention groups chartered in Virginia are subject to all of the provisions of the Unfair Trade Practices Act. Risk retention groups chartered outside of the Commonwealth, on the

other hand, are only subject to certain provisions of the Unfair Trade Practices Act. These provisions include §§38.2-500 through 38.2-504, 38.2-506, 38.2-510, and 38.2-512. Section 38.2-510 pertains to unfair claims settlement practices. The other provisions deal with deceptive, false, or fraudulent acts or practices.

Companies issuing home protection contracts must also adhere to the provisions in the Unfair Trade Practices Act found in Chapter 5 of Title 38.2. In addition, the State Corporation Commission may issue an order, pursuant to §38.2-2612, calling for the company to cease and desist from engaging in certain unfair trade practices such as making false or misleading statements, either oral or written, in connection with the sale, offer to sell, or advertisement of a home protection contract.

Financial Regulation

The Bureau is responsible for licensing, monitoring, and ensuring the financial solvency of insurance companies doing business in Virginia. Homeowners insurance companies, home protection insurance companies, and risk retention groups operating in Virginia must meet certain financial and operating requirements as established in Title 38.2 of the Code of Virginia. Risk retention groups chartered outside of the Commonwealth are not subject to the same requirements as risk retention groups chartered in Virginia but do have to file certain financial information with the Bureau such as a plan of operation and financial statements.

REGULATION OF WARRANTIES

While homeowners insurance contracts, home protection insurance contracts, and liability insurance contracts, including those issued by risk retention groups chartered in Virginia, are regulated by the State Corporation Commission, home warranties provided by builders are not. A warranty may be defined as a statement made by a seller or manufacturer of goods which provides assurance that the goods being sold are as represented and as promised. "It is made... to induce the sale and is relied on by the buyer."⁶

The Bureau has long taken the position that any warranty provided by a manufacturer or seller of a product or service is not considered insurance. However, when a contract providing a warranty on goods is sold by a party other than the manufacturer or seller of the goods, it becomes insurance and is regulated by the State Corporation Commission. (See Administrative Letter 1982-10 in Appendix IV of this report.) This is consistent with the position taken by a number of other state insurance departments. Also, Chapter 26 of the Insurance Code, which regulates home protection companies, exempts the following from the provisions of the chapter:

1. Performance guarantees given by either (i) the builder of a home or (ii) the manufacturer, seller, or lessor of the property that is the subject of the contract if no identifiable charge is made for the guarantee; and
2. Any service contract, guarantee, or warranty intending to guarantee or warrant the repairs or service of a home appliance, component, part, or system that is issued (i) by a person who has sold, serviced, repaired, or provided replacement of the appliance, component, part, or system at the time of or prior to issuance of the service contract, guarantee or warranty if such person does not engage in the business of a home protection company or (ii) by a home protection company which sells such service contracts, guarantees or warranties in Virginia and has a net worth in excess of \$100 million.

Laws governing warranties are found in the Uniform Commercial Code of every state. These laws describe how an express warranty is created and also establish standards for implied warranties.⁷ In Virginia, these laws are set forth in Title 8.2 of the Code of Virginia and generally apply to movable goods. In addition to each state's Uniform Commercial Code, the federal government regulates warranties. In 1975, Congress passed the Magnuson-Moss Warranty-Federal Trade Commission Improvement Act which governs products made after July 4, 1975. This law is enforced by the Federal Trade Commission and applies to consumer products which are defined as tangible personal property for personal, family, or household use, including fixtures. A few states have enacted additional warranty laws which, in some cases, go beyond the Magnuson-Moss Act in

providing consumer protection.⁸

In 1991, the General Assembly enacted the Extended Service Contract Act. This Act is set forth in §§59.1-435 through 59.1-441 of the Code of Virginia. Home warranties are not covered under this Act since it pertains only to tangible personal property, not real estate. (A copy of this Act is shown in Appendix V.) The Virginia Department of Agriculture and Consumer Services regulates extended service contracts which may be sold with products such as appliances and electronic equipment. An extended service contract is a written agreement which is in effect for at least one year whereby the purchaser is indemnified against the cost of repair or replacement of a consumer product which is defective in material or workmanship in return for the payment of a segregated charge by the purchaser. Anyone selling these contracts must register with the Department of Agriculture and Consumer Services and post a bond. The department logs complaints, mediates disputes resulting from the sale of these contracts, and conducts investigations to determine whether there have been any violations of the law.

Transactions involving real property are governed under Title 55 (Property and Conveyances). Section 55-70.1 establishes standards for implied warranties on new homes. Subsection B of this section requires a vendor, who is in the business of building or selling dwellings, to warrant to the vendee in every contract for the sale of a new dwelling, that the dwelling with all its fixtures is sufficiently (i) free from structural defects so as to pass without objection in the trade; (ii) constructed in a workmanlike manner so as to pass without objection in the trade; and (iii) fit for habitation. The term "structural defects," as used in this section, means a defect or defects which reduce the stability or safety of the structure below accepted standards or which restrict the normal use thereof. As stated in §55-70.1, the warranty extends for a period of one year from the date of transfer of record title or the vendee's taking possession, whichever occurs first. In 1992, this section was amended to extend the required one-year warranty to a period of five years for structural defects in the foundation of a new dwelling.

As previously noted, the Department of Agriculture and Consumer Services has no jurisdiction over home warranties even though it regulates extended service contracts. The Department of Professional and Occupational Regulation (formerly the Department of Commerce) also has no jurisdiction over home warranties and does not regulate these products or the providers of these products. The State Corporation Commission's Bureau of Insurance may become involved in consumer complaints involving home warranties even though it has no direct regulatory control over these warranties. The Bureau's regulatory authority extends over the liability insurance coverage which is provided as a back up for the warranty.

INSURANCE COMPANY SURVEYS

Purpose of Surveys

The Bureau sent a survey to the top twenty-five writers of homeowners insurance in Virginia, all home protection companies licensed in Virginia, and three risk retention groups which provide "back up" insurance for home warranties sold in Virginia. The purpose of the surveys was to determine the following:

- (1) whether any companies provide coverage for damage to foundations and/or other home structural components resulting from shrink-swell soil conditions;
- (2) whether any companies provide coverage for damage to foundations and/or other home structural components resulting from something other than shrink-swell soil conditions;
- (3) the number of claims reported to the companies for damage to foundations and/or other home structural components in Virginia between January 1, 1990 and December 31, 1992;
- (4) the number of claims paid, the total dollar amount paid, the number of claims still pending, the number of claims denied, and the reasons given for the denials for claims reported for damage to foundations and/or other home structural components; and
- (5) whether the claims data compiled by the companies could be broken down to show (i) the number of claims for damage to foundations and/or other home structural components resulting from shrink-swell soil conditions, as compared to (ii) the number of claims for damage to foundations and/or other home structural components resulting from something other than shrink-swell soil conditions.

A summary of the Bureau's findings is provided below.

Homeowners Insurance Company Survey

Responses were received from all twenty-five homeowners insurance companies that were surveyed. Only one company indicated that coverage is provided under one of their homeowners policies for damage to foundations and/or other home structural components resulting from shrink-swell soil conditions. Allstate Insurance Company reported that their "Delux Plus" policy offers, for an additional premium, Earth Movement Coverage. This coverage provides protection resulting from earth movement, including but not limited to sinking, rising, shifting, expanding, or contracting of the earth. Allstate's remaining homeowners policies offer Earthquake Coverage which, for an additional premium, specifically covers earthquake or volcanic eruption.

The other twenty-four homeowners insurance companies reported that their policies exclude coverage for earth movement including earth sinking, rising, or shifting. Some policies also

specifically mention expanding or contracting under the exclusion for earth movement. Also cited in most of the policies was the provision stating that coverage is not provided for settling, cracking, shrinking, bulging, or expansion of pavements, patios, foundations, floors, roofs, or ceilings. Some of the companies also cited the provision that excludes coverage due to freezing, thawing, pressure or weight of water or ice to a fence, pavement, patio, swimming pool, or foundation.

When asked if coverage was provided for damage to foundations and/or other home structural components resulting from something other than shrink-swell soil conditions, all twenty-five companies said "yes." Some companies explained that this coverage was provided except as specifically excluded under the policy. Other companies mentioned that coverage would be provided as a result of a direct physical loss from a covered event such as a fire, windstorm, or damage by a vehicle.

When asked if any claims were reported to the company for damage to foundations and/or other home structural components in Virginia between January 1, 1990 and December 31, 1992, the majority of the companies indicated that they did not keep records of this detailed information. Two companies said they knew claims had been reported but that the specific number of losses reported was unknown. One company indicated that five claims had been reported and all were denied. According to the company, three of these may have been related to shrink-swell soil because they were located in Chesterfield County. Another company indicated that one claim had been reported and denied. According to the company, this was not related to shrink-swell soil.

Home Protection Company Survey

Responses were received from each of the four home protection companies that are licensed and in good standing in Virginia. Two of these companies (American Home Shield of Virginia, Inc. and HAA of Virginia, Inc.) indicated that their contract does not provide coverage for damage to foundations and/or other home structural components. They also stated on the survey that they do not keep any records which would indicate whether claims for this type of damage had been reported between January 1, 1990 and December 31, 1992.

The other two companies (United One Home Protection Corporation of Virginia and Mid-Atlantic Insurance Corporation) indicated that they do provide coverage for damage to foundations and other home structural components. United One Home Protection Corporation of Virginia, hereinafter referred to as United One, indicated that coverage would be provided for damage resulting from shrink-swell soil or something other than shrink-swell soil but only under certain conditions as stated in their contract as follows:

Physical damage to the following designated load-bearing

portions of the Home caused by failure of such load-bearing portions which affect load-bearing functions; walls, floors, ceiling, foundation. Regardless of the number of claims, the maximum aggregate liability of the Service for any structural claim is \$3,000.00. With regard to roof; leaks only, including asphalt shingles, rolled roofing, flashing. Regardless of the number of claims made hereunder, the maximum aggregate limit of the Service for roof repairs is \$300.00 for the life of the contract.

United One provides Buyer's Coverage and Seller's Coverage. Seller's Coverage begins the eleventh day after the date of listing, or earlier as provided in the contract, and continues until the expiration of the initial listing period (up to 180 days), until close of sale, or until listing is cancelled, whichever occurs first. Buyer's Coverage extends twelve months from the date of closing as stated in the contract and is renewable every year. The maximum aggregate liability for any structural claim, therefore, is \$3000 per year and the maximum aggregate limit for roof repairs is \$300 per year.

United One stated on the survey that 31 claims had been reported in Virginia between January 1, 1990 and December 31, 1992 for damage to foundations and/or other home structural components. Three of these claims were paid, twenty-two were denied, and six were still pending. The total dollar amount paid to settle the three paid claims was \$1,890. The reason given for the twenty-two denied claims was that the damage was not structural as defined by the contract. The company reported that it was not able to distinguish between claims that had resulted from shrink-swell soil and claims that had resulted from something other than shrink-swell soil.

It should be noted that United One is no longer actively marketing its contract that provides coverage for structural damage.

Mid-Atlantic Insurance Corporation trading as HW10, hereinafter referred to as Mid-Atlantic, writes a ten-year home protection policy. The premium for this policy is paid for by the builder. Coverage is provided to the homeowner for major structural defects for all ten years. However, the company states in the policy that, during the first year of coverage, it will in its sole discretion repair, replace, or pay the actual cost to correct any major structural defect. The policy states that if a major structural defect occurs in the first year of coverage, all repairs necessary to bring the home into compliance with the company's "Construction Standards" will be made. During the second year of coverage and also for years three through ten, however, the policy adds another criteria that it will in its sole discretion repair, replace, or pay the reasonable and actual cost to correct any major structural defect. The term "major structural defect" is defined in the policy as "actual physical damage to the load-bearing portions of the home, caused by failure of such load-bearing portions, which affects their load-

bearing function to the extent that the home becomes unsafe or unsanitary." The policy further states that the term "unsafe or unsanitary" as it applies to major structural defects is limited to the repair of oil, electric, gas, waste, and plumbing lines; ductwork; heating systems, and other items damaged by the major structural defect which affect the health and safety of its occupants. The term "load-bearing components" is defined in the policy as beams; columns; footings and foundation systems; floor systems; girders; lintels; roof framing systems; and load-bearing walls and partitions. Roof sheathing was added to this provision when the contract was revised in November, 1991; however, this revision was not filed with the Bureau of Insurance.

Mid-Atlantic lists twenty-one exclusions in its home protection policy. One of these is stated as follows:

Any damage, defect, or breakdown in the home, or any component thereof, during the period when such home or component is covered by a manufacturer's, contractor's, or builder's warranty. Notwithstanding the foregoing exclusion, any damage, defect, or breakdown that would otherwise be covered hereby if it were not for this exclusion, will be covered pursuant to all of the other terms, conditions, and exclusions hereof if the warrantor does not comply with the obligations set forth in the warranty.

Mid-Atlantic reported on the Bureau's survey that coverage is provided under its contract for damage to foundations and/or other home structural components resulting from shrink-swell soil conditions or resulting from something other than shrink-swell soil conditions.

Mid-Atlantic stated that twenty-six claims had been reported in Virginia between January 1, 1990 and December 31, 1992 for damage to foundations and/or other home structural components. Five of these claims were paid and twenty-one were denied. The total dollar amount paid to settle the five paid claims was \$35,135. When asked what reasons were given for the denials, the company responded "policy language." The company also indicated that, since the region in which coverage is provided (the Tidewater area of Virginia) does not have shrink-swell soil conditions, no claims have been reported for this type of damage.

Risk Retention Group Survey

Responses were received from all three risk retention groups that were surveyed. These were HOW Insurance Company, A Risk Retention Group, which is chartered in Virginia; National Home Insurance Company (A Risk Retention Group) which is chartered outside of Virginia; and Western Pacific Mutual Insurance, A Risk Retention Group, which is also chartered outside of Virginia.

HOW Insurance Company, A Risk Retention Group, hereinafter referred to as HOW, provides liability insurance for its member builders. Premium for this coverage is paid by the builder.

HOW's contract provides Builder Default Coverage and Major Structural Defect Coverage. Under the Builder Default Coverage, HOW agrees to repair or replace defective items covered under the builder's limited warranty or pay the homeowner the reasonable cost of such repair or replacement if the builder defaults under the warranty. This coverage terminates two years from its commencement date. Major Structural Defect Coverage provides coverage for major structural defects that first occur during the term of the Major Structural Defect Coverage. This coverage begins after the expiration of the builder's two-year limited warranty. The Major Structural Defect Coverage terminates eight years from its commencement date, thus providing coverage for years three through ten. Under this coverage, HOW agrees to repair or replace the defective items or pay the homeowner the reasonable cost of such repair or replacement.

HOW stated on the survey that coverage is provided for damage to foundations and/or other home structural components resulting from shrink-swell soil or resulting from something other than shrink-swell soil but only under certain conditions. The repair of a major structural defect is limited (i) to the repair of damage to the load-bearing portions of the home which are necessary to restore their load-bearing function; and (ii) to the repair of those items of the home damaged by the major structural defect which made the home unsafe, unsanitary or otherwise unlivable. The term "major structural defect" is defined as actual physical damage to any of the following designated load-bearing portions of the home caused by failure of such load-bearing portions which affects their load-bearing functions to the extent that the home becomes unsafe, unsanitary or otherwise unlivable:

1. Foundation systems and footings;
2. Beams;
3. Girders;
4. Lintels;
5. Columns;
6. Walls and partitions;
7. Floor systems; and
8. Roof framing systems.

The term "unsafe, unsanitary or otherwise unlivable" is not defined.

HOW stated on the Bureau's survey that a total of 1,804 claims had been reported in Virginia between January 1, 1990 and December 31, 1992 for damage to foundations and/or other home structural components. The company indicated that it could not distinguish between claims that had resulted from shrink-swell soil and claims that had resulted from something other than shrink-swell soil. Among the 1,804 claims that were reported, 406 were paid, 1,362 were denied, and 36 were still pending. The company stated that (i) a total dollar amount of \$1,701,436 had been paid to-date for claims reported and settled during the three-year time period; (ii) \$440,148 had been paid in loss

adjustment expenses on all reported claims; and (iii) \$46,059 had been paid as partial payments on the pending claims. The company listed the following as examples of the more common reasons for denying claims:

1. Defect did not meet the definition of major structural defect;
2. Defect is governed by the exclusions;
3. Damage did not exceed the deductible;
4. Defect reported in years 3-10 was a first year item for which coverage had expired.

HOW's program lists twenty exclusions, including one which states that coverage will not be applicable to any insurance claim not filed in a manner set forth in the section entitled "How to Make a Claim." One of these provisions requires the homeowner to notify HOW in writing of a claim no later than 30 days after the expiration of the applicable coverage term.

National Home Insurance Company (A Risk Retention Group), hereinafter referred to as National Home, provides insurance coverage if a builder fails for any reason to perform its warranty obligations under the Home Buyers Warranty limited warranty program. Premium for this coverage is paid by the builder. National Home agrees to perform the obligations of the builder under the same terms and conditions set forth in the warranty with respect to the builder. Coverage is provided for structural defects which occur during the ten year period beginning on the day that settlement or closing occurs. A five-year extended warranty term can be selected by the builder which provides coverage for structural damage which occurs during the extended five-year term. This term begins on the first day of the eleventh year after the day that settlement or closing occurs. Structural damage is defined as actual physical damage to the following designated load-bearing portions of the home caused by failure of such load-bearing portions which affect their load-bearing function to the extent that the home becomes unsafe, unsanitary or otherwise unlivable:

1. Foundation systems and footings;
2. Beams;
3. Girders;
4. Lintels;
5. Columns;
6. Roof sheathing on FHA-financed homes only;
7. Walls and partitions;
8. Floor systems; and
9. Roof framing systems.

Examples of non-load-bearing elements which are deemed not to have structural defect potential include roof shingles, sheathing, and tar paper. The term "unsafe, unsanitary or otherwise unlivable" is not defined.

National Home stated on the Bureau's survey that coverage is provided for damage to foundations and/or other home structural components resulting from shrink-swell soil or resulting from something other than shrink-swell soil but only under certain conditions. As stated on the survey, such coverage is subject to the company's exclusions. One of these exclusions is stated as follows:

Subsidence or soil movement which was not reasonably predictable through reasonable soil testing or other geological investigation at the time of construction of the home. This exclusion does not apply to any home provided with a FHA/VA or FmHA loan or on any home that has received a soil investigation conducted in accordance with Home Buyers Warranty Underwriting Requirements.

National Home stated that 78 claims had been reported in Virginia between January 1, 1990 and December 31, 1992 for damage to foundations and/or other home structural components. Nine of these were paid, 49 were denied, and 20 were still pending. The total dollar amount paid to settle these claims was \$61,241. Most of the denials, according to the response given on the survey, were due to the fact that the defects did not meet the criteria for coverage under the structural defect definition. When asked if the company could distinguish which claims were due to shrink-swell soil, the company answered "yes." Out of the 78 claims that had been reported, 17 resulted from shrink-swell soil. Of these, six were paid at a total of \$31,441, and eleven were denied. As noted above, denials were based on the fact the defects claimed did not meet the criteria for coverage under the structural defect definition.

On July 2, 1993, the State Corporation Commission issued an order granting a motion for temporary injunction against National Home. As of June 30, 1993, the company is temporarily enjoined from issuing any new policies or any new certificates or other evidences of coverage in the Commonwealth of Virginia until the company restores its surplus to the minimum amount required by its state of domicile. An exception is made if the company has received a notification of start and a deposit premium on or before June 30, 1993, or if a member builder has obtained a building permit on or before June 30, 1993 and the company receives a notification of start and a deposit premium prior to September 1, 1993.

Western Pacific Mutual Insurance Company, A Risk Retention Group, hereinafter referred to as Western Pacific, provides insurance coverage insuring the builder's performance during the first two years of the limited warranty insurance program and also provides protection against major structural defects during the third through the tenth years of the program. Premium for this coverage is paid for by the builder. This program is administered by Residential Warranty Corporation which is neither the warrantor nor the insurer. "Major structural defect" is defined as actual physical damage to the following specified

load-bearing segments of the home, caused by a failure of such segments which affects their load-bearing functions to the degree that the home becomes unsafe or unlivable:

1. Roof framing members and systems (rafters and trusses);
2. Floor systems (joists);
3. Bearing walls and partitions;
4. Columns;
5. Lintels;
6. Girders;
7. Load-bearing beams; and
8. Foundation systems and footings.

The term "unsafe or unlivable" is not defined.

A HUD/VA addendum is added for FHA financed homes only. This addendum states that the failure of roof sheathing shall also be deemed to be a major structural defect.

An Active Soils Addendum is also attached to the limited warranty agreement which stipulates certain homeowner maintenance responsibilities for homes constructed on active soils, i.e. soils with a high clay content. Failure to execute these post-construction maintenance requirements voids the warranty coverage. A copy of this addendum is shown in Appendix VI of this report.

Residential Warranty Corporation (RWC) answered the Bureau's survey on behalf of Western Pacific and explained that coverage was provided for damage to foundations and/or other home structural components resulting from shrink-swell soil, subject to certain exclusions. One exclusion mentioned on the survey was as follows:

Loss or damage caused by soil movement, including subsidence, expansion or lateral movement of the soil (excluding flood and earthquake) which is covered by any other insurance or for which compensation is granted by legislation.

Another section was mentioned which states that the agreement provides warranty coverage in excess of coverage provided under other warranties or insurance, whether collectible or not.

When asked if coverage was provided for damage to foundations and/or other home structural components resulting from something other than shrink-swell soil, the company answered "yes" as long as the damage meets the definition of major structural defect and is not excluded. The following exclusions were listed:

Loss or damage resulting from the purchaser's failure to minimize or prevent such loss or damage in a timely manner.

Loss or damage resulting from or made worse by dampness, condensation, or heat build-up caused by failure of the

purchaser to maintain proper ventilation.

In addition to these exclusions, the company mentioned that there was a condition in the warranty agreement which stated that the applicability of the warranty standards was further conditioned upon the purchaser's proper maintenance of the home to prevent damage due to neglect, abnormal use, or improper maintenance.

RWC reported that 15 claims had been filed in Virginia between January 1, 1990 and December 31, 1992 for structural damage. Three claims were paid (although one of these was still pending), eleven claims were denied, and one additional claim did not exceed the homeowner's deductible. The reason given for the denial of the eleven claims was that the criteria for a major structural defect had not been met. The company indicated that it had paid a total of \$61,517 to-date to settle these claims, including the amounts paid for the claim that was still open.

When asked if the company could separate, from among the claims that had been reported, those claims that were linked to shrink-swell soil conditions, the company answered "yes" and indicated that two such claims had been alleged by homeowners but that they had not been paid. One was denied because a stoop that was separating from the house due to dirt settling was not structurally attached to the foundation. The other claim was denied because water had seeped into the basement through a crack less than 1/8" thick. The survey stated that water seepage is a standard applicable to the first year of coverage only and that the crack was less than the standards set forth in the limited warranty agreement.

MARKETING MATERIALS USED BY REAL ESTATE FIRMS

At the request of the chief patron of the study resolution, Delegate John Watkins, the Bureau contacted several real estate firms to determine what information is given to home buyers or potential home buyers by real estate agents regarding the protection afforded by home warranties and home protection companies. Real estate agents are permitted to sell home protection insurance contracts, as are home builders, without becoming licensed as insurance agents. This is authorized under §38.2-2609 of the Code of Virginia. Out of ten real estate firms contacted in the Richmond area, five responded to the Bureau's request. These were:

- (1) ERA Pro Realty, Inc.;
- (2) Bowers, Nelms, and Fonville;
- (3) Virginia Landmark Corporation;
- (4) Coldwell Banker Executive Properties; and
- (5) RE/MAX Executives, Inc.

ERA offers a Buyer Protection Plan through First American Insurance Company which is a licensed property and casualty insurance company authorized to sell home protection insurance pursuant to §38.2-2602. Coverage is not provided by this insurance company for structural damage. The ERA plan provides protection against the breakdown of major working components in a newly purchased home. Subject to certain exclusions and limitations, the plan covers heating equipment, interior plumbing fixtures, interior plumbing systems, interior electrical system, water heater, duct work, air conditioning, water softener, appliances, and domestic well pump. ERA also offers a Seller Protection Plan through the same insurance company. This provides protection to sellers while the house is on the market. Neither plan offers coverage for major structural defects.

Bowers, Nelms, and Fonville sells coverage to home buyers and home sellers through HAA of Virginia, Inc. The HAA policy does not cover major structural defects, but does provide coverage for the following items, subject to certain limitations and exclusions:

- (1) Electrical system
- (2) Plumbing system
- (3) Refrigerator
- (4) Microwave (built-in)
- (5) Oven/range
- (6) Washer/dryer
- (7) Hot water heater
- (8) Dishwasher
- (9) Water softener
- (10) Garage door opener
- (11) Central vacuum
- (12) Trash compactor (built-in)
- (13) Garbage disposal
- (14) Ceiling fans

Coverage for home buyers only is also provided for the following items:

- (1) Central air conditioning
- (2) Wall unit air conditioners
- (3) Heating system
- (4) Accessible ductwork

Like Bowers, Nelms, and Fonville, Virginia Landmark sells coverage to home buyers and home sellers through HAA of Virginia, Inc. The HAA policy does not cover major structural defects.

Coldwell Banker offers home buyers and sellers their Best Buyer Home Protection Plan which they sell through American Home Shield of Virginia, Inc. Subject to certain limitations and exclusions, the plan covers the following items:

- (1) Plumbing system
- (2) Heating system - available only to buyer after close of sale
- (3) Electrical system
- (4) Water heater
- (5) Dishwasher
- (6) Range/oven
- (7) Garbage disposal
- (8) Built-in microwave
- (9) Trash compactor
- (10) Well pump
- (11) Ductwork - available only to buyer after close of sale

The plan also makes other optional coverages available to home buyers. It does not provide coverage for structural damage.

RE/MAX sells coverage through American Home Shield of Virginia, Inc. and United One Home Protection Corporation of Virginia. Neither plan provides coverage for major structural defects. Both plans offer buyer and seller coverage.

The Richmond Association of Realtors was also contacted for assistance with this study. According to the president of the association, programs offered by real estate companies provide coverage for mechanical systems and do not cover structural damage. This confirmed the information collected from the five real estate firms that responded to the Bureau's request for information. The association also indicated that home warranties provided by builders and the "back up" insurance for these warranties are generally not marketed through real estate agents but are marketed by the builders themselves. This was confirmed by the Home Builders Association of Richmond which indicated that the only exception to this would be where a site agent might market a warranty on behalf of a builder he or she represents.

The Richmond Association of Realtors also provided the Bureau with the latest legislative changes that were passed during the 1992 and 1993 Sessions of the General Assembly.

Effective July 1, 1993, §55-518 of the Code of Virginia was amended to require the builder of a new dwelling to disclose in writing to the purchaser all known material defects which would constitute a violation of any applicable building code. The law also states that this disclosure does not abrogate any warranty or any other contractual obligations the builder may have to the purchaser.

As noted earlier in this report, §55-70.1 of the Code of Virginia, which pertains to implied warranties on new homes, was amended in 1992. Subsection B of this section requires a vendor, who is in the business of building or selling dwellings, to warrant to the vendee in every contract for the sale of a new dwelling, that the dwelling with all its fixtures is sufficiently (i) free from structural defects so as to pass without objection in the trade; (ii) constructed in a workmanlike manner so as to pass without objection in the trade; and (iii) fit for habitation. The 1992 amendment extended the required one-year warranty to a period of five years for structural defects in the foundation of new dwellings. The term "structural defects," as used in this section, means a defect or defects which reduce the stability or safety of the structure below accepted standards or which restrict the normal use thereof.

Copies of §§55-70.1 and 55-518 are contained in Appendix VII of this report.

INSURANCE COMPANY INVESTIGATIONS

Purpose of Investigations

In addition to surveying the insurance companies for this study, the Bureau conducted an investigation of the two home protection companies that had indicated on the surveys that their contract provides coverage for structural damage. These two companies were United One Home Protection Corporation of Virginia, Inc. and Mid-Atlantic Insurance Corporation. The Bureau also conducted an investigation of HOW Insurance Company, A Risk Retention Group which was the only risk retention group being studied in this report that is chartered in Virginia. The purpose of the investigations was to review the companies' claims settlement and adjustment practices. The following information summarizes the Bureau's findings.

Claims Practices

The Bureau reviewed all 31 claims that had been reported to United One Home Protection Corporation of Virginia, Inc. between January 1, 1990 and December 31, 1992 for damage to foundations and/or other home structural components in Virginia. The Bureau also reviewed all 26 claims that had been reported to Mid-Atlantic Insurance Corporation during the same time frame for the same type of damage. Of the 1,804 claims that had been reported to HOW Insurance Company, A Risk Retention Group, for the same time period, the Bureau reviewed a total of 50 structural defect claims. These 50 claims were randomly selected from the Richmond/Chesterfield area.

Generally, the companies being investigated denied claims for structural defects because one or more of the conditions which trigger the coverage had not yet been met. In many cases, the loss of load-bearing capacity had not yet rendered the home unsafe, unsanitary or unlivable. In other cases, although the load-bearing component had sustained damage, the load-bearing capacity had not yet been affected.

For two of the companies, coverage determination is a four-step process.

- 1) There must be actual physical damage;
- 2) The damage must be to a load-bearing component;
- 3) The load-bearing capacity must be affected;
- 4) As a result, the home is unsafe or unsanitary.

One company's definition incorporates only the first three steps. Thus, the threshold for coverage in that company's contract is much lower than that of either of the other two companies.

During the investigation, the examiners saw examples of claims for major structural defects denied because the defect had not yet rendered the home unsafe, unsanitary or unlivable, as required by the contract. The homeowner would make a second claim for the same defect. At this point, the claim would be paid because the condition had been met. In a similar example, a claim had been made for three rotted porch columns. After inspecting the damage, the company denied repairs to two of the columns because they were still supporting the roof; the damage to the third, which had lost at least one-half of its effective strength, was repaired. All of these claims were handled in accordance with the companies' contracts.

One company stated that they had come to the realization that if it was clear that the condition would worsen and the unsafe, unsanitary or unlivable condition would be met, it was more economical to pay the claim initially than to wait for the damage to get worse.

There were some differences in what each company characterized as a "load-bearing portion" of the home. One company's contract contained a short definition, i.e. walls, floors, ceiling and foundation. Since no additional qualifications were placed on the definition, this contract language could be interpreted very broadly. However, the company appeared to adjust the claims as if the contract language were more specific and more limited. For example, the company denied a claim arising from a leaking skylight. The contract states: "With regard to roof; leaks only, including asphalt shingles, rolled roofing, flashing." The claim was denied because skylights are not specifically included. However, Chapter 26 of the Code of Virginia requires that all home protection contracts specifically set forth all exclusions and limitations respecting the extent of coverage. It would appear that since the skylight is a part of the roof, any leaks around it would be covered because they are not specifically excluded. The other two companies' contracts were found to be more specific; the contracts listed a larger number of components which qualified as "load-bearing." One of these companies included a list of components which did not qualify.

Another problem with structural claims noted by the examiners had to do with who makes the determination whether the loss is covered. Two of the companies investigated rely on engineers to determine if actual physical damage to a load-bearing component has affected the load-bearing capacity to the extent the home has become unsafe or unsanitary (one company adds "or otherwise unliveable"). The third company uses its repair contractors to determine if the load-bearing function has been affected. In some cases, the engineer or contractor appears to overstep his duties and interprets the contract. In one such case, the engineer's report stated that damage to a chimney did not qualify for structural defect coverage because a chimney is "not part of the house's structural system." The applicable contract covered losses to footings and foundation systems. The

chimney's foundation system failed causing the damage. There is nothing in the contract that requires the load-bearing component to be part of the "house's structural system." The company initially relied on the engineer's interpretation of the contract and denied the claim.

Another area which appeared to give the companies problems is the extent of the company's obligation to make repairs or replace damaged items. It is not clear whether the company has to repair/replace only the damaged load-bearing component or whether other items are covered as well. It is also not clear whether these items have to render the home unsafe or unsanitary in order to qualify for coverage. Equally unclear is whether damage caused by the repair effort itself is covered, i.e. replacing custom wallpaper on a wall that was just repaired.

As a result of these investigations, the Bureau found instances of claims handling practices which appear to be in violation of the standards set forth in Virginia insurance laws. Since these were outside the scope of this study, they will be addressed in market conduct examination reports prepared by the Bureau of Insurance at a later date.

CONCLUSION

Generally, coverage for damage to foundations and other home structural components resulting from shrink-swell soil conditions is excluded under homeowners insurance policies. In addition, coverage for this type of damage is provided for in some home protection contracts but is excluded in others. The Bureau found that, generally, the three companies investigated for this study are paying claims in accordance with their policy provisions. Any instances of claims settlement practices which are not in compliance with policy provisions on file with the Bureau or which are not in compliance with the standards set forth in the unfair claims settlement practices laws of Title 38.2 of the Code of Virginia will be cited in the Bureau's market conduct reports.

ENDNOTES

(1) "Facts You Should Know About Shrink/Swell Soils," prepared by the Chesterfield County Commission on Soils and Foundations, distributed by the Chesterfield County News and Public Information Office.

(2) Bernard E. Schmelz, "Shrink/Swell Soils -- Myths and Reality," 1993 Chesterfield Almanac.

(3) Lane B. Ramsey, County Administrator, "Chesterfield County and Shrink-Swell Soils -- An Innovative Solution to an Old Problem."

(4) Ibid.

(5) Ibid.

(6) Donald S. Malecki, et al., Commercial Liability Risk Management and Insurance, Vol. I (Malvern, PA: American Institute for Property and Liability Underwriters, Inc., 1986), p 87.

(7) James J. Lorimer, et al., The Legal Environment of Insurance, Vol II (Malvern, PA: American Institute for Property and Liability Underwriters, Inc., 1981), p. 294.

(8) Ibid.

APPENDIX I

STATE CORPORATION COMMISSION - BUREAU OF INSURANCE
FINANCIAL REGULATION

WRITERS OF INSURANCE WITH STATUS - 00,04,03,

PFS010

DATE: 07/21/93

PAGE 1

COMPANY NAME AND ADDRESS	NAIC	PREMIUMS WRITTEN
STATE FARM FIRE AND CASUALTY COMPANY 112 EAST WASHINGTON STREET BLOOMINGTON IL 61701	25143	85,572,519
ALLSTATE INSURANCE COMPANY ALLSTATE PLAZA NORTHBROOK IL 60062	19232	58,128,074
NATIONWIDE MUTUAL FIRE INSURANCE COMPANY ONE NATIONWIDE PLAZA COLUMBUS OH 43216	23779	53,887,787
UNITED SERVICES AUTOMOBILE ASSOCIATION USAA BUILDING SAN ANTONIO TX 78284	25941	31,797,405
GOVERNMENT EMPLOYEES INSURANCE COMPANY ONE GEICO PLAZA WASHINGTON DC 20076	22063	14,373,204
ERIE INSURANCE EXCHANGE 100 ERIE INSURANCE PLACE ERIE PA 16530	26271	10,922,919
VIRGINIA FARM BUREAU MUTUAL INSURANCE COMPANY P.O. BOX 27552 RICHMOND VA 23261	26034	9,889,587
STATE FARM GENERAL INSURANCE COMPANY 112 EAST WASHINGTON STREET BLOOMINGTON IL 61701	25151	8,685,032

STATE CORPORATION COMMISSION - BUREAU OF INSURANCE
FINANCIAL REGULATION

WRITERS OF INSURANCE WITH STATUS - 00,04,03,

DATE: 07/21/93

PF5010

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COMPANY		NAIC	PREMIUMS WRITTEN
NAME AND ADDRESS			
USAA CASUALTY INSURANCE COMPANY		25968	3,231,982
USAA BUILDING			
SAN ANTONIO	TX 78286		
PHOENIX INSURANCE COMPANY THE		25623	6,394,545
ONE TOWER SQUARE			
HARTFORD	CT 06183		
TRAVELERS INDEMNITY COMPANY THE		25658	5,363,089
ONE TOWER SQUARE			
HARTFORD	CT 06183		
STANDARD FIRE INSURANCE COMPANY THE		19070	6,154,975
151 FARMINGTON AVENUE			
HARTFORD	CT 06156		
LIBERTY MUTUAL FIRE INSURANCE COMPANY		23035	5,515,747
175 BERKELEY STREET			
BOSTON	MA 02117		
LUMBERMENS MUTUAL CASUALTY COMPANY		22977	5,240,018
1 KEMPER DRIVE			
LONG GROVE	IL 60049		
VIRGINIA MUTUAL INSURANCE COMPANY		18791	4,363,201
7501 BOULDERS VIEW DRIVE (300)			
RICHMOND	VA 23225		
PRUDENTIAL PROPERTY AND CASUALTY INSURANCE COMPANY		32352	4,313,090
23 MAIN STREET			
HOLMDEL	NJ 07733		

STATE CORPORATION COMMISSION - BUREAU OF INSURANCE
FINANCIAL REGULATION

WRITERS OF INSURANCE WITH STATUS - 00,04,03,

DATE: 07/21/95

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PAGE 3

COMPANY NAME AND ADDRESS	NAIC	PREMIUMS WRITTEN
AETNA CASUALTY AND SURETY COMPANY THE 151 FARMINGTON AVENUE HARTFORD CT 06156	19035	4,236,129
AMERICAN BANKERS INSURANCE COMPANY OF FLORIDA 11222 QUAIL ROOST DRIVE MIAMI FL 33157	10111	5,863,795
CINCINNATI INSURANCE COMPANY THE P.O. BOX 145496 CINCINNATI OH 45250	10677	5,594,385
UNITED STATES FIDELITY AND GUARANTY COMPANY P. O. BOX 1138 LEGAL DEPT.--COMPLIANCE OFFICER BALTIMORE MD 21203	25887	3,416,302
VIGILANT INSURANCE COMPANY 100 WILLIAM STREET NEW YORK NY 10038	20397	2,979,363
FIDELITY AND GUARANTY INSURANCE UNDERWRITERS INC 100 LIGHT STREET, P.O. BOX 1138 BALTIMORE MD 21203	25879	2,800,136
HARLEYSVILLE MUTUAL INSURANCE COMPANY 355 MAPLE AVENUE HARLEYSVILLE PA 19458	14165	2,711,392
ARMED FORCES INSURANCE EXCHANGE PO BOX G FORT LEAVENWORTH KS 66027	41459	2,701,527

STATE CORPORATION COMMISSION - BUREAU OF INSURANCE
FINANCIAL REGULATION

WRITERS OF INSURANCE WITH STATUS - 00,04,05,
DATE: 07/21/93

PFS010

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COMPANY		
NAME AND ADDRESS	NAIC	PREMIUMS WRITTEN
FIDELITY AND GUARANTY INSURANCE COMPANY	35386	2,581,082
100 LIGHT STREET, P.O. BOX 1138		
BALTIMORE	MD 21203	

APPENDIX II

1992 PREMIUMS WRITTEN IN VIRGINIA
HOME PROTECTION INSURANCE COMPANIES

Date: 08/27/93

Company Name and Address	NAIC Number	Premiums Written
HAA of Virginia, Inc. P. O. Box 9200 Hollywood, FL 33084	35513	\$2,111,705
Mid-Atlantic Insurance Corporation 2117 Smith Avenue Chesapeake, VA 23320	11533	\$ 586,010
United One Home Protection Corporation of Virginia 2313 East Atlantic Boulevard Pompano Beach, FL 33062	35700	\$ 519,655
American Home Shield of Virginia, Inc. 90 S. East Street Santa Rosa, CA 95404	46493	\$ 439,426
Realsafe Corporation of Virginia, Inc. 12500 Fairlakes Circle Suite 300 Fairfax, VA 22033	00047	\$ - 0 -

APPENDIX III

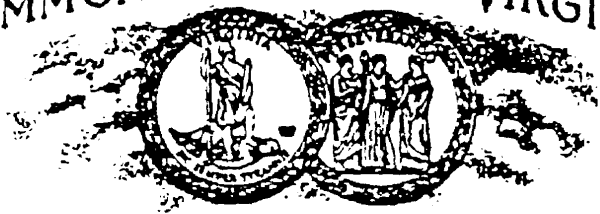
**1992 PREMIUMS WRITTEN IN VIRGINIA
FOR RISK RETENTION GROUPS STUDIED IN THIS REPORT**

Date: 08/25/93

Company Name and Address	NAIC Number	Premiums Written
HOW Insurance Company, A Risk Retention Group 1110 North Glebe Road Arlington, VA 22201	41246	\$1,366,155
National Home Insurance Company (A Risk Retention Group) 2675 S. Abilene Street Aurora, CA 80014-2363	44016	\$ 966,711
Western Pacific Mutual Insurance Company, A Risk Retention Group 1571 Race Street Denver, CO 80206	40940	\$ 203,502

APPENDIX IV

COMMONWEALTH OF VIRGINIA



JAMES M. THOMSON
COMMISSIONER OF INSURANCE

BOX 1157
RICHMOND, VA. 23209
TELEPHONE (804) 786-37

STATE CORPORATION COMMISSION BUREAU OF INSURANCE May 20, 1982

Administrative Letter 1982-10

TO: All Automobile Manufacturers, Automobile Dealers Licensed in Virginia, Property and Casualty Insurers Licensed in Virginia, and Persons Issuing Motor Vehicle Service Contracts in Virginia.

RE: Motor Vehicle Service Contracts

The purpose of this letter is to address the area of "motor vehicle service contracts", "extended automobile warranties", "extended service contracts", "limited service agreements", and similar instruments indemnifying consumers for mechanical breakdown of motor vehicles.

There appears to be some confusion in the minds of consumers, insurers, providers of motor vehicle service contracts, and other interested parties as to the legal status of such contracts. Additionally, there has been considerable regulatory interest in these contracts on the part of a number of states in light of the insolvency of North American Dealer Group, a major provider of motor vehicle service contracts.

Under section 38.1-21 of the Code of Virginia, motor vehicle and aircraft insurance is defined to include, among other things, loss or damage resulting from any cause to motor vehicles. Pursuant to this section, the Bureau of Insurance has approved "mechanical breakdown insurance" policy forms filed for use in the Commonwealth of Virginia by several licensed motor vehicle insurers. Typically, these policies provide coverage for the cost of repair or replacement of specified parts of a motor vehicle resulting from mechanical breakdown. Mechanical breakdown is usually defined as the inability of a part to perform the function for which it was designed.

It has come to the Bureau's attention that numerous other entities, including motor vehicle manufacturers, motor vehicle dealers, and independent third parties are offering for sale, selling, or providing within the Commonwealth contracts called "motor vehicle service contracts" or some similar name, which contracts are virtually identical in coverage to mechanical breakdown insurance policies offered by licensed motor vehicle insurers. Some motor vehicle service contracts do differ from mechanical breakdown insurance policies in that they contain provisions that would not be permitted if the contracts were filed for approval as insurance policies. Notwithstanding such differences, the Bureau, after a careful examination of numerous motor vehicle service contract forms, is unable to perceive any substantive difference between motor vehicle service contracts and mechanical breakdown insurance policies.

In light of the substantial identity of motor vehicle service contracts and mechanical breakdown insurance, it is the opinion of the Bureau of Insurance that such

contracts, by whatever named called, are policies of mechanical breakdown insurance if offered by a person other than the manufacturer or seller of the covered motor vehicle.

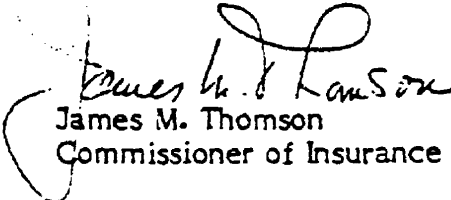
Accordingly, the Bureau of Insurance is of the opinion that the offer to sell, the sale, or the providing of such contracts within the Commonwealth of Virginia by a person other than the manufacturer or seller of the covered vehicle constitutes the transacting of an insurance business, and that persons transacting such business must be licensed as insurers under applicable provisions of Title 38.1 of the Code of Virginia.

The Bureau is of the opinion that contracts offered by the manufacturer or seller of the covered motor vehicle are more in the nature of warranties than of insurance. The primary risk of loss under such contracts must remain with and be borne by the manufacturer or seller, or the contract will be deemed to be an insurance policy.

The Bureau is also aware that some dealers are issuing motor vehicle service contracts and then purchasing contractual liability or reimbursement insurance policies to cover or back up their losses under the contracts. The Bureau regulates these back up policies as contractual liability insurance and there is no objection by the Bureau to this arrangement.

The Bureau of Insurance hopes that this administrative letter eliminates the confusion regarding the legal status of motor vehicle service contracts and similar arrangements. The Bureau suggests that all parties issuing, selling, or providing such contracts familiarize themselves as quickly as possible with the applicable provisions of the Virginia insurance laws, as the Bureau intends to enforce all applicable laws dealing with the sale of this type of insurance.

Sincerely,


James M. Thomson
Commissioner of Insurance

JMT/rvt

APPENDIX V

for pay-per-call services: (i) the pay-per-call number called; (ii) the date, time, and length of the call; and (iii) the amount charged. (1991, cc. 608, 630.)

§ 59.1-432. **Regulations.** — The Board is authorized to prescribe reasonable regulations in order to implement provisions in this chapter relating to pay-per-call service advertising or solicitation. These regulations shall be adopted, amended, or repealed in accordance with the Administrative Process Act (§ 2-6.14:1 et seq.). (1991, cc. 608, 630.)

§ 59.1-433. **Investigations.** — A. The Commissioner may, with respect to pay-per-call service advertising or solicitation:

1. Make necessary public and private investigations within or without this Commonwealth to determine whether any person has violated the provisions of this chapter, or any rule, regulation, or order issued pursuant to this chapter;

2. Require or permit any person to file a statement in writing, under oath or otherwise as the Commissioner determines, as to all facts and circumstances concerning the matter under investigation; and

3. Administer oaths or affirmations, and upon such motion or upon request of any party, may subpoena witnesses, compel their attendance, take evidence, and require the production of any matter that is relevant to the investigation, including the existence, description, nature, custody, condition, and location of any books, documents, or other tangible things and the identity and location of persons having knowledge of relevant facts, or any other matter reasonably calculated to lead to the discovery of material evidence.

B. Any proceeding or hearing of the Commissioner pursuant to this chapter, in which witnesses are subpoenaed and their attendance required for evidence to be taken, or any matter is to be produced to ascertain material evidence, shall take place within the City of Richmond.

C. If any person fails to obey a subpoena or to answer questions propounded by the Commissioner and upon reasonable notice to all persons affected thereby, the Commissioner may apply to the Circuit Court of the City of Richmond for an order compelling compliance. (1991, cc. 608, 630.)

§ 59.1-434. **Enforcement; penalties.** — Any violation of this chapter shall constitute a prohibited practice under the provisions of § 59.1-200 and shall be subject to any and all of the enforcement provisions of the Virginia Consumer Protection Act (§ 59.1-196 et seq.) of this title. (1991, cc. 608, 630.)

CHAPTER 34.

EXTENDED SERVICE CONTRACT ACT.

Sec.	Sec.
59.1-435. Definitions.	59.1-439. Investigations.
59.1-436. Registration; fees; exemptions.	59.1-440. Production of records.
59.1-437. Bond or letter of credit required.	59.1-441. Violations of chapter; penalty.
59.1-438. Regulations.	

§ 59.1-435. **Definitions.** — As used in this chapter, unless the context requires a different meaning:

"Board" means the Virginia Board of Agriculture and Consumer Services.

"Commissioner" means the Commissioner of the Department of Agriculture and Consumer Services or his designee.

"Consumer product" means tangible personal property primarily used for personal, family, or household purposes.

"Extended service contract" or "contract" means a written agreement which is in effect for at least one year whereby the purchaser is indemnified against the cost of repair or replacement of a consumer product which is defective in material or workmanship in return for the payment of a segregated charge by the purchaser.

"Extended service contract provider" or "provider" means any person or entity other than a public service corporation supervised by the State Corporation Commission, who is the original manufacturer or seller and who solicits, offers, advertises, or executes extended service contracts.

"Purchaser" means a person who enters into an extended service contract with an extended service contract provider. (1991, c. 654.)

The numbers of §§ 59.1-435 through 59.1-441 were assigned by the Virginia Code Commission, the numbers in the 1991 act having been 59.1-429 through 59.1-435.

§ 59.1-436. **Registration; fees; exemptions.** — A. It shall be unlawful for any extended service contract provider to offer, advertise, or execute or cause to be executed by the purchaser any extended service contract for a consumer product in this Commonwealth unless the provider at the time of the solicitation, offer, advertisement, sale, or execution of a contract has been properly registered with the Commissioner. The registration shall (i) disclose the address, ownership, and nature of business of the provider; (ii) be renewed annually; and (iii) be accompanied by a fee of \$100 per registration and annual renewal.

B. All fees shall be remitted to the State Treasurer and shall be placed to the credit and special fund of the Virginia Department of Agriculture and Consumer Services to be used in the administration of this chapter.

C. Any matter subject to the insurance regulatory authority of the State Corporation Commission pursuant to Title 38.2 shall not be subject to the provisions of this chapter.

D. Licensed or registered motor vehicle dealers, as defined in § 46.2-1500, shall not be subject to the provisions of this chapter. (1991, c. 654.)

§ 59.1-437. **Bond or letter of credit required.** — A. Every extended service contract provider, before it is registered, shall file and maintain with the Commissioner, in form and substance satisfactory to him, a bond with corporate surety, from a company authorized to transact business in the Commonwealth or a letter of credit from a bank insured by the Federal Deposit Insurance Corporation, in the amount of \$10,000. Additional bond or letter of credit amounts shall be similarly filed with the Commissioner and shall be adjusted from time to time, in accordance with the following schedule:

Total Amount of Unexpired Extended Service Contracts	Amount of Bond or Letter of Credit
\$0 to \$50,000	\$10,000
\$50,001 to \$300,000	\$40,000
\$300,001 to \$750,000	\$65,000
\$750,001 or more	\$90,000

The total amount of unexpired extended service contracts shall be the total consideration paid by all purchasers to the extended service provider for all extended service contracts currently in effect.

B. The bond or letter of credit required by subsection A of this section shall be in favor of the Commonwealth for the benefit of purchasers of extended

service contracts for consumer products in the event that the extended service contract provider does not fulfill its obligations under such contracts for any reason, including insolvency or bankruptcy.

C. The aggregate liability of the bond or letter of credit to all persons for all breaches of the conditions of the bond or letter of credit shall in no event exceed the amount of the bond or letter of credit. The bond or letter of credit shall not be cancelled or terminated except with the consent of the Commissioner. (1991, c. 654.)

§ 59.1-438. Regulations. — The Board is authorized to prescribe reasonable regulations in order to implement provisions in this chapter relating to extended service contracts. These regulations shall be adopted, amended, or repealed in accordance with the Administrative Process Act (§ 9-6.14:1 et seq.). (1991, c. 654.)

§ 59.1-439. Investigations. — A. The Commissioner may, with respect to extended service contracts:

1. Make necessary public and private investigations within or without this Commonwealth to determine whether any person has violated the provisions of this chapter or any rule, regulation, or order issued pursuant to this chapter;

2. Require or permit any person to file a statement in writing, under oath or otherwise as the Commissioner determines, as to all facts and circumstances concerning the matter under investigation; and

3. Administer oaths or affirmations, and upon motion or upon request of any party, may subpoena witnesses, compel their attendance, take evidence, and require the production of any matter that is relevant to the investigation, including the existence, description, nature, custody, condition, and location of any books, documents, or other tangible things and the identity and location of persons having knowledge of relevant facts, or any other matter reasonably calculated to lead to the discovery of material evidence.

B. Any proceeding or hearing of the Commissioner pursuant to this chapter, in which witnesses are subpoenaed and their attendance required for evidence to be taken, or any matter produced to ascertain material evidence, shall take place within the City of Richmond.

C. If any person fails to obey the subpoena or to answer questions propounded by the Commissioner and upon reasonable notice to all persons affected thereby, the Commissioner may apply to the Circuit Court of the City of Richmond for an order compelling compliance. (1991, c. 654.)

§ 59.1-440. Production of records. — Every extended service contract provider, upon written request of the Commissioner, shall make available to the Commissioner its extended service contract records for inspection and copying to enable the Commissioner to reasonably determine compliance with this chapter. Every provider shall maintain a true copy of each contract executed between the provider and a purchaser, and each contract shall be maintained for its term. (1991, c. 654.)

§ 59.1-441. Violations of chapter; penalty. — A. Any extended service provider who knowingly and willfully violates any provision of this chapter shall be guilty of a Class 3 misdemeanor.

B. Any violation of the provisions of this chapter shall constitute a prohibited practice pursuant to the provisions of § 59.1-200 and shall be

§ 59.1-441~

TRADE AND COMMERCE

§ 59.1-441

subject to any and all of the enforcement provisions of the Virginia Consumer Protection Act (§ 59.1-196 et seq.) of this title. (1991, c. 654.)

Cross references. — As to punishment for Class 3 misdemeanors, see § 18.2-11.

APPENDIX VI

D.2 ACTIVE SOILS ADDENDUM

Homeowner Maintenance Responsibilities for Homes Constructed On Active Soils

Soils having a high clay content can expand and contract when variations occur in the moisture content of the soils. Where seasonal moisture changes in the sub-surface soils are common, it is the responsibility of the homeowner to provide proper ongoing maintenance. Although foundations are specifically designed for soil conditions in each area, conditions may be encountered that were not revealed by sub-surface exploration and testing.

Additionally, improper homeowner maintenance can adversely affect the performance and structural integrity of any foundation constructed on active soils. These post-construction practices are beyond the control of the design engineer and the builder.

To minimize the probability of movement and displacement in the foundation caused by moisture content variations, the following post-construction maintenance and requirements must be executed. Failure to do so by the homeowner will void the warranty coverage provided by Residential Warranty Corporation.

1. A final grade certificate has been issued for the lot on which your home is located. This confirms that the final grade, as established by the builder, meets the warranty requirements. The homeowner is responsible for maintaining such grades in accordance with the final grade certificate. The grade around the foundation shall be maintained by the homeowner in such a manner that surface drainage is away from the foundation, and shall not permit water to pond or become trapped in localized areas against the foundation. This can cause variations in moisture content that can damage the foundation.
2. Watering shall be done in a uniform systematic manner as equally as possible on all sides of the foundation to keep the soil moist, NOT SATURATED. Areas of soil that do not have ground cover may require more moisture as they are more susceptible to evaporation, causing a moisture content imbalance.
3. During extreme hot and dry periods, close observations should be made around the foundation to insure adequate watering is being provided, preventing soil from separating or pulling back from the foundation.
4. Gutters and downspouts shall be maintained to prevent injection of moisture into the soil from roof run-off in localized areas. Downspout extensions shall be maintained to discharge a minimum of five feet away from the foundation wall.
5. Studies show that trees planted within twenty (20) feet of the foundation can damage the structural integrity of the foundation. Trees planted in close proximity to the foundation can develop a root system which can penetrate beneath the foundation and draw moisture from the soil. Areas around trees will require more water in periods of extreme drought. If the homeowner plants a tree closer than twenty (20) feet to the foundation, warranty coverage may be affected. Precautionary measures such as the installation of a root shield or root injection system should be taken to maintain moisture equilibrium.
6. Placing flower gardens and beds or shrubs next to the foundation and watering these areas heavily will generally result in a net increase of the soil moisture content in that localized area. This may result in a soil expansion in that localized area of the foundation. The homeowner must maintain a balanced soil moisture content around the perimeter of the foundation.

APPENDIX VII

ARTICLE 3.

*Effect of Certain Expressions in Deeds and Leases.***§ 55-70. Words "with general warranty," "with special warranty" and "with English covenants of title" construed.**

Applied in *Barzee v. Trammel*, 63 Bankr. 878 (Bankr. E.D. Va. 1986).

§ 55-70.1. Implied warranties on new homes. — A. In every contract for the sale of a new dwelling, the vendor shall be held to warrant to the vendee that, at the time of the transfer of record title or the vendee's taking possession, whichever occurs first, the dwelling with all its fixtures is, to the best of the actual knowledge of the vendor or his agents, sufficiently (i) free from structural defects, so as to pass without objection in the trade, and (ii) constructed in a workmanlike manner, so as to pass without objection in the trade.

B. In addition, in every contract for the sale of a new dwelling, the vendor, if he be in the business of building or selling such dwellings, shall be held to warrant to the vendee that, at the time of transfer of record title or the vendee's taking possession, whichever occurs first, the dwelling together with all its fixtures is sufficiently (i) free from structural defects, so as to pass without objection in the trade, (ii) constructed in a workmanlike manner, so as to pass without objection in the trade, and (iii) fit for habitation.

C. The above warranties implied in the contract for sale shall be held to survive the transfer of title. Such warranties are in addition to, and not in lieu of, any other express or implied warranties pertaining to the dwelling, its materials or fixtures. A contract which waives, modifies or excludes some or all of the warranties contained in this section shall be valid, but the words used to waive, modify or exclude such warranties shall be conspicuously (as defined in § 8.1-201 (10)) set forth on the face of such contract, and shall specify the particular warranty or warranties to be waived, modified or excluded.

D. If there is a breach of warranty under this section, the vendee, or his heirs or personal representatives in case of his death, shall have a cause of action against his vendor for damages.

E. The warranty shall extend for a period of one year from the date of transfer of record title or the vendee's taking possession, whichever occurs first, except that the warranty pursuant to subdivision (i) of subsection B for the foundation of new dwellings shall extend for a period of five years from the date of transfer of record title or the vendee's taking possession, whichever occurs first. Any action for its breach shall be brought within two years after the breach thereof. As used in this section, the term "new dwelling" shall mean a dwelling or house which has not previously been occupied for a period of more than sixty days by anyone other than the vendor or the vendee or which has not been occupied by the original vendor or subsequent vendor for a cumulative period of more than twelve months excluding dwellings constructed solely for lease. The term "new dwelling" shall not include a condominium or condominium units created pursuant to Chapter 4.2 (§ 55-79.39 et seq.) of this title.

F. The term "structural defects," as used in this section, shall mean a defect or defects which reduce the stability or safety of the structure below accepted standards or which restrict the normal use thereof. (1979, c. 282; 1988, c. 394; 1992, c. 431.)

§ 55-518. Exemptions. — A. The following are specifically excluded from the provisions of this chapter:

1. Transfers pursuant to court order including, but not limited to, transfers ordered by a court in administration of an estate, transfers pursuant to a writ of execution, transfers by foreclosure sale, transfers by a trustee in bankruptcy, transfers by eminent domain, and transfers resulting from a decree for specific performance.

2. Transfers to a beneficiary of a deed of trust by a trustor or successor in interest who is in default; transfers by a trustee under a deed of trust pursuant to a foreclosure sale, or transfers by a beneficiary under a deed of trust who has acquired the real property at a sale conducted pursuant to a foreclosure sale under a deed of trust or has acquired the real property by a deed in lieu of foreclosure.

3. Transfers by a fiduciary in the course of the administration of a decedent's estate, guardianship, conservatorship, or trust.

4. Transfers from one or more co-owners solely to one or more other co-owners.

5. Transfers made solely to any combination of a spouse or a person or persons in the lineal line of consanguinity of one or more of the transferors.

6. Transfers between spouses resulting from a decree of divorce or a property settlement stipulation pursuant to the provisions of Title 20.

7. Transfers made by virtue of the record owner's failure to pay any federal, state, or local taxes.

8. Transfers to or from any governmental entity of public or quasi-public housing authority or agency.

9. Transfers involving the first sale of a dwelling.

B. Notwithstanding the provisions of subdivision 9 of this section, the builder of a new dwelling shall disclose in writing to the purchaser thereof all known material defects which would constitute a violation of any applicable building code. Such disclosure shall not abrogate any warranty or any other contractual obligations the builder may have to the purchaser. The disclosure required by this subsection may be made on the disclosure form described in § 55-519. The builder may not satisfy the requirements of this subsection by the use of the disclaimer statement described in § 55-519. (1992, c. 717; 1993, c. 824.)

The 1993 amendment added the subsection A designation, and added subsection B.