STATE OF FLORIDA
DIVISION OF ADMINISTRATIVE HEARINGS

STATE FARM FLORIDA INSURANCE COMPANY, Petitioner, vs. DEPARTMENT OF INSURANCE, Respondent.	)	Case No. 02-3107

RECOMMENDED ORDER

Upon due notice, William R. Cave, an Administrative Law Judge for the Division of Administrative Hearings, held a formal hearing in this matter on January 13 through 17, 2003, and February 17, 2003, in Tallahassee, Florida.

APPEARANCES

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STATEMENT OF THE ISSUE

Should the Department of Insurance (now known as the Department of Financial Services, Office of Insurance Regulation) (Department) approve three insurance endorsement forms that State Farm Florida Insurance Company (State Farm) filed on November 15, 2001?

PRELIMINARY STATEMENT

On November 15, 2001, State Farm filed for approval pursuant to Section 627.410, Florida Statutes, three proposed endorsement forms (FE-5397, FE-5398, and FE 5399, Fungus (Including Mold) Exclusion Endorsement (endorsements)) to its already approved policy forms on file with the Department.

The endorsements, as distinguished by number, apply to different policy forms.

By letter dated June 28, 2002, the Department notified State Farm that the previous approval of the endorsements, approved by operation of law, was withdrawn as being in violation of Sections 627.411(1)(b) and 626.9641(1)(b), Florida

Statutes. The letter also advised State Farm of its rights pursuant to Sections 120.569 and 120.57, Florida Statutes.

On July 18, 2002, State Farm filed a Petition for Administrative Hearing Involving Disputed Issues of Fact with the Department requesting a formal hearing pursuant to Sections 120.569(1) and 120.57(1), Florida Statutes. Upon receipt of State Farm's request for a formal proceeding the matter was referred to the Division of Administrative Hearings (Division) for the assignment of an Administrative Law Judge and for the conduct of a formal hearing.

On December 4, 2002, the Department moved for leave to amend its original disapproval letter. The motion was granted on December 5, 2002. The Department's amended disapproval letter, which the Department back-dated to June 28, 2002, reiterates the previously alleged basis for disapproval and cites two additional purported bases for disapproval: (1) the alleged violation of Section 626.9641(1)(b), Florida Statutes, itself constitutes a violation of Section 627.411(1)(a), Florida Statutes; and (2) the endorsements because they exclude coverage that, "through custom and usage has become a standard or uniform provision" in Florida, violate Section 627.412(2), Florida Statutes.

At the hearing, State Farm presented the testimony of James Orsulak, James Horton, Richard Haberer, Jeffery McCarty, and

Richard Corbett. State Farm's Exhibits numbered 1 through 11, 22 through 25, 44 through 121, 218, 219, 227, 234 through 241, 298, 324, 325, 331 through 350, and 352 through 355 were admitted in evidence. The Department presented the testimony of Shirley Kerns and Charles Tutwiler. The Department's Exhibits 1 through 25 and 27 through 40 were admitted in evidence.

A nine-volume Transcript of this proceeding was filed with the Division on March 3, 2003. The parties requested, and were granted additional time to file proposed recommended orders with the understanding that any time constraint imposed under Rule 28-106.216(1), Florida Administrative Code, was waived in accordance with Rule 28-106.216(2), Florida Administrative Code. The parties timely filed their Proposed Recommended Orders under the extended time frame.

FINDINGS OF FACT

Upon consideration of the oral and documentary evidence adduced at the hearing, the following relevant findings of fact are made:

1. State Farm is a domestic insurance company that the Department has licensed to transact property and casualty insurance in the State of Florida.

2. The Department is the state agency charged with the duty to regulate insurers doing business in the State of Florida.

3. State Farm offers five types of homeowners' policies that have been approved for use in Florida, an FP-7921 (HO1), FP-7923 (HO3), FP-7924 (HO4), FP-7925 (HO5-Extra), and FP-2926 (HO6). The HO1 is a "named perils" policy and provides coverage only for those perils specifically named in the policy. This policy is not offered in other states, and in Florida accounts for less than one percent of all of all policies in force. The HO3, HO5, and HO6 policies are known as "open perils" policies providing coverage for all risks unless specifically excluded by the policy. Although similar to HO3, the HO5 policy provides somewhat broader coverage with respect to settlement provisions. The HO6 policy is specifically geared toward condominium owners and the HO4 policy is the policy form that applies to renters. Of all the policies offered in Florida, the HO3 is the most widely used policy form and will be quoted from and used as the exemplar in this Recommended Order.

4. The HO3 policy contains introductory provisions entitled "Declarations" and "Definitions," and is then divided into two coverage sections, Sections I and II. Section I refers to property coverage and with Section II referring to liability coverage. Section I is divided into a number of subcategories including the following: Coverage A (Dwelling), Coverage B (Personal Property), Section C (Loss of Use), Additional Coverage, Losses Insured, Losses Not Insured, and Conditions.

Following the Section II provisions there are additional sections entitled "Section I and II-Conditions" and a section entitled "Optional Provisions."

5. The HO3 policy provides coverage under Coverage A (Dwelling) for all risks of loss unless it is a "loss not insured." As stated in the policy: "We insure for accidental direct physical loss to the property described in Coverage A, except as provided in SECTION I - LOSSES NOT INSURED." (Emphasis in the original.) However, coverage for personal property (Coverage B) does not provide such "open perils" coverage. Rather, it provides coverage only for 16 named perils, contains a number of limitations on personal property that it does cover, and reflects a number of personal property items that it does not cover.

6. All of State Farm's homeowners' policies currently provide some limited coverage relating to mold. Although the policies exclude mold as a covered peril, they provide some limited coverage for mold-related losses resulting from covered perils, such as a covered water loss that causes mold-related damage.

7. Historically, there have been exclusions in property insurance for ordinance of law, earth movement, flood, war, the neglect of the insured, and nuclear hazard. Mold that resulted from a covered peril has historically not been excluded.

8. On November 15, 2001, State Farm filed three proposed endorsement forms (Fungus (Including Mold) Exclusion Endorsement): (1) FE-5397 for use with HO1 policies; (2) FE-5398, for use with HO3, HO5, and HO6 policies; and (3) FE-5399 for use with HO4 policies. The homeowners' policies, which the endorsements were to apply, had been previously approved by, and were on file with the Department, in accordance with Section 627.410, Florida Statutes. The goal of the endorsements was to eliminate mold coverage from State Farm's existing homeowners policies in Florida.

9. State Farm's current rates do not include the cost of providing the mold coverage that the endorsements seek to exclude. However, there is insufficient evidence to establish facts to show that State Farm would need to substantially raise its rates to include those costs.

10. Before filing the mold-exclusion endorsements, State Farm entered into discussions with the Department about giving policyholders the choice of buying back some of the to-be-excluded mold coverage through buy-back endorsements (buy-backs).

11. State Farm filed its buy-backs in June 2002, after failing to work out a solution with the Department that would have allowed for their approval.

12. Although the Department disapproved the buy-backs in December 2002, State Farm has committed itself to provide policyholders with the optional buy-backs, if the exclusions are approved.

13. If the exclusion endorsements are approved along with the buy-back provisions, any cost increase would be restricted to those policyholders who choose to purchase mold coverage through a buy-back.

14. State Farm's filings of mold-exclusion endorsements are consistent with a nationwide effort by State Farm Fire & Casualty Insurance Company, an affiliate of State Farm to eliminate mold coverage in homeowners policies.

15. In Florida, State Farm's endorsements accomplish the complete elimination of mold coverage chiefly through the addition of a new exclusion for fungus, including mold, within "SECTION I - LOSSES NOT INSURED." (Emphasis in the original.) The endorsements, when coupled with the underlying policy, state in relevant part as follows:

> 2. We do not insure under any coverage for any loss which would not have occurred in the absence of one or more of the following excluded events. We do not insure for such loss regardless of: (a) the cause of the excluded event; or (b) other causes of the loss; or (c) whether other causes acted concurrently or in any sequence with the excluded event to produce the loss; or (d) whether the event occurs suddenly or gradually, involves isolated or widespread

damage, arises from natural or external forces, or occurs as result of any combination of these:

* * *

g. Fungus. (Emphasis in the original.) (The text of the endorsement is underlined.)

16. The endorsements delete all references to the term mold found in SECTION 1 - LOSSES INSURED. (Emphasis in the original.)

17. The endorsements define fungus as follows:

> "fungus" means any type or form of fungus, including mold, mildew, mycotoxins, spores, scents or byproducts produced or released by fungi. (Emphasis furnished.)

18. This total exclusion of mold coverage, using language clearly encompassing all manner of causation and occurrence, replaces the mold exclusions in the existing policies that do not use such broad language. The difference between the post- and pre-endorsement policies can be seen from comparing the above-quoted endorsement as incorporated into HO3 policy on the one hand, with the mold exclusions as they currently exist in the HO3 policy on the other hand. While the endorsements totally exclude coverage for fungus (mold), and deny payment for mold damage historically provided to insureds, the endorsements are not ambiguous, notwithstanding the testimony offered by the Department to the contrary, which lacks credibility.

19. The endorsements do not add coverage. Instead, the endorsements eliminate coverage for mold that currently exists. However, this fact alone does not render the endorsements inconsistent, misleading, or deceptive when the endorsements are read in their entirety along with the remaining provisions of the policies.

20. State Farm's endorsements were initially deemed approved pursuant to Section 627.410, Florida Statutes, which provides that an endorsement filed with the Department is deemed approved if it is not approved or disapproved within 30 days, or 45 days if there has been an extension, of its filing..

21. By letter dated June 28, 2002, the Department withdrew its deemed approval of the three endorsements and notified State Farm of its basis for disapproval.

22. The Department's original disapproval letter cites three bases for disapproval. The Department asserts that State Farm's endorsements: (1) contain ambiguities in violation of Section 627.411(1)(b), Florida Statutes; (2) deceptively affect the risk purported to be assumed in the general coverage of the contract, also in violation of Section 627.411(1)(b), Florida Statutes; and (3) deny policyholders the right to obtain "comprehensive coverage" as that term is used in Section 626.9641(1)(b), Florida Statutes, which is part of the policyholders' bill of rights.

23. On December 4, 2002, the Department moved for leave to amend its original disapproval letter. The motion was granted. The Department's amended disapproval letter, which the Department back-dated to June 28, 2002, reiterates the previously alleged bases for disapproval and cites two additional bases for disapproval: (1) the alleged violation of Section 626.9641(1)(b), Florida Statutes, itself constitutes a violation of Section 627.411(1)(a), Florida Statutes; and (2) the endorsements, because they exclude coverage that "through custom and usage has become a standard or uniform provision" in Florida, violate Section 627.412(2), Florida Statutes.

24. There is insufficient evidence to establish facts to show that the provision for mold coverage has, through custom and usage, become a standard or uniform provision.

25. Likewise, there is insufficient evidence to establish facts to show that there is a "natural association between mold and water."

26. In the fall of 2001, the Department began receiving a large influx of filings seeking to exclude or severely limit coverage for mold. Including State Farm's filing, the Department received between 400 and 450 filings representing between 200 and 250 insurers primarily between October 1, 2001, through the end of 2002.

27. In the face of the inordinate number of filings, the Department sought input from all sectors of the public. The Department met with insurers and other interested persons and held four public forums around the state to determine the impact the filings would have on insurance contracts, the industry, and the market place.

28. In the mean time, the Department routinely sought waivers from the insurers of the statutory review period set forth in Section 627.410(2), Florida Statutes, and additionally requested that insurers withdraw their filings.

29. Insurers were advised by the Department that failure to waive the statutory review period or to withdraw their filings would result in the filing being disapproved.

30. The Department initially approved the endorsements to limit or exclude mold coverage of three insurers: USAA, Maryland Casualty, and American Strategic. However, the Department withdrew its approval for each of these companies in letters dated September 18, 2002.

31. The Department asserts that it does not have a policy to disapprove filings simply because they discuss mold or seek to limit or exclude coverage for claims involving mold damage. The Department admits that it is required to examine all filings based upon the statutory scheme. However, the Department has not approved a single one of the over 450 filings, regardless of

the language or structure of the endorsements. The simple fact is that the Department had a policy from the fall of 2001 through December 16, 2002, imposing a moratorium on the exclusion or limitation of mold coverage. The Department altered that policy on December 17, 2002, when it entered into a settlement with Florida Farm Bureau General Insurance Company (Farm Bureau), wherein Farm Bureau's endorsement was approved allowing a reduction in mold coverage from policy limits to a sub-limit of $10,000.00 per occurrence, $20,000.00 annual aggregate. The Department's previous position that policies offered to Florida's consumers should not be significantly reduced was abandoned at that time. There was insufficient evidence to establish facts to show that the $10,000.00 coverage was a reasonable amount of coverage for the vast majority of claims for mold damage.

32. The endorsements seek to limit or exclude coverage for mold that has existed for decades. There is scant Florida experience to support the need for limitations or exclusions on mold coverage. Even so, the Department cannot disapprove endorsement forms without authority to do so. There is no statutory authority mandating mold coverage to the extent of policy limits or otherwise in order for policyholders to have comprehensive coverage.

33. Beginning September 15, 2001, the Department did not approve a single mold endorsement seeking to exclude or limit coverage for mold as a resulting loss from a covered peril until December 17, 2002, when it approved a filing by Farm Bureau as a part of a settlement of an administrative proceeding in which the parties were awaiting ruling after a final hearing.

CONCLUSIONS OF LAW

34. The Division of Administrative Hearings has jurisdiction over the parties and the subject matter of this proceeding. Sections 120.569 and 120.57(1), Florida Statutes.

35. State Farm has the burden of proving by a preponderance of the evidence that the Department should approve the endorsements. Young v. Department of Community Affairs, 625 So. 2d 831 (Fla. 1993).

36. Section 627.411(1)(a),(b), Florida Statutes, provides as follows in relevant part:

> (1) The Department shall disapprove any form filed under 627.410, or withdraw any previous approval thereof, only if the form:
>
> (a) Is in any respect in violation of, or does not comport with, this code.
>
> (b) Contains or incorporates by reference, where such incorporation is otherwise permissible, any inconsistent, ambiguous, or misleading clauses, or exceptions and conditions which deceptively affect the risk purported to be assumed in the general coverage of the contract. (Emphasis furnished.)

37. Pursuant to Section 627.419(1), Florida Statutes, "[e]very insurance contract shall be construed according to the entirety of its terms and conditions as set forth in the policy and as amplified, extended or modified by any . . . endorsement thereto."

38. In this case, the endorsements are not inconsistent with the coverage in the policies. Although the endorsements totally eliminate coverage for mold damage, they do not contain any provisions that conflict with the policies. To interpret the term "inconsistent" in Section 627,411(1)(b), Florida Statutes, as prohibiting any difference between a policy and its endorsement, would mean that an insurer could never use an endorsement to amend or modify a policy.

39. The endorsements, read in their entirety, in conjunction with the policies are not ambiguous, misleading, or deceptive. There is nothing ambiguous, misleading or deceptive about the endorsements eliminating mold coverage. Clearly, the purpose of the endorsements is to eliminate mold coverage

40. The endorsements do not violate Section 627.411(1))b), Florida Statutes, and should be approved if the Department had disapproved them only on that basis. However, the Department also disapproved the endorsements on grounds that they violated Section 626.9641(1)(b), Florida Statutes, which in itself was a

violation of Section 627.411(1)(a), Florida Statutes, and that because the endorsements excluded coverage that, "through custom and usage has become a standard or uniform provision" in Florida they violate Section 627.412(2), Florida Statutes.

41. Section 626.9641(1)(b), Florida Statutes, states as follows in pertinent part:

> (1) The principles expressed in the following statements shall serve as standards to be followed by the department in exercising its powers and duties, in exercising administrative discretion, in dispensing administrative interpretations of the law, and in promulgating rules:
>
> * * *
>
> (b) Policyholders shall have the right to obtain comprehensive coverage.

42. The Department argues that the policyholder's bill of rights provides authority for it to disapprove the endorsements because they take away valuable coverage that has existed for decades, thereby interfering with the right of policyholders to comprehensive coverage. This argument is without merit. Therefore, since the Department has failed to prove a violation of Section 626.9641(1)(b), Florida Statutes, there is no violation of Section 627.411(1)(a), Florida Statutes.

43. Section 627.412(2), Florida Statutes, provides as follows:

> (2) No policy shall contain any provision inconsistent with or contradictory to any

> standard or uniform provision used or required to be used, but the department may approve any substitute provision which is, in its opinion, not less favorable in any particular to the insured or beneficiary that the provisions otherwise required.

Section 627.412(2), Florida Statutes, has to be read in conjunction with Section 627.412(1), Florida Statutes, which requires that all insurance contracts contain provisions mandated by the Insurance Code and failure to include that provision is a violation of Section 627.412(2), Florida Statutes. In this case, the policy endorsements do not "contain any provision inconsistent with or contradictory to any standard or uniform provision used or required to be used."

44. Section 120.52(15), Florida Statutes, defines a rule as "each agency statement of general applicability that implements, interprets, or prescribes law or policy . . . ."

45. Section 120.52(8), Florida Statutes. states as follows in pertinent part:

> A grant of rulemaking authority is necessary by not sufficient to allow an agency to adopt a rule; a specific law to be implemented is also required. An agency may adopt only rules that implement, interpret or make specific the particular powers and duties granted by the enabling statute. No agency shall have authority to adopt a rule only because it is reasonably related to the purpose of the enabling legislation and is not arbitrary and capricious or is within the agency's class of powers and duties, nor shall an agency have the authority to implement statutory provisions setting forth

general legislative intent or policy. Statutory language granting rulemaking authority or generally describing the powers and functions of an agency shall be construed to extend no further than implementing or interpreting the specific powers and duties conferred by the same statute.

46. Section 120.57(1)(e), Florida Statutes, states as follows in relevant part:

(e)1. Any agency action that determines the substantial interests of a party and that is based on an unadopted rule is subject to de novo review by and administrative law judge.
2. The agency action shall not be presumed valid or invalid. The agency must demonstrate that the unadopted rule:
a. Is within the powers, functions, and duties delegated by the Legislature or, if the agency is operating pursuant to authority derived from the State Constitution, is within that authority;
b. Does not enlarge, modify, of contravene the specific provisions of law implemented;
c. Is not vague, establishes adequate standards for agency decisions, or does not vest unbridled discretion in the agency;
d. Is not arbitrary or capricious;
e. Is not being applied to the substantially affected party without due notice;
f. Is supported by competent and substantial evidence; and
g. Does not impose excessive regulatory costs on the regulated person, county, or city.

47. The Department's decision to disapprove the endorsements because they restrict coverage that insurers have historically provided to policyholders is a rule as defined

under Section 120.52(15), Florida Statutes. It is a statement of general applicability because the Department has effectively declared a moratorium on such endorsements. The decision interprets and prescribes law to the extent that the Department relies on Subsections 626.9641(1)(b), 627.411(1)(a), (b), and 627.412(2), Florida Statutes.

48. As a rule that has not been adopted pursuant to the rulemaking procedures of Chapter 120, Florida Statutes, the Department's unadopted rule, including its most recent rendition of the unadopted rule (mandating a minimum of $10,000.00 in coverage for mold), violates Subsections 120.57(1)(e)2.a., 120.57(1)(e)(2)b., and 120.57(1)(e)2.d., Florida Statutes, for the following reasons: (a) There is no statutory or rule definition of a comprehensive homeowner's policy; (b) The policyholder's bill of rights, as do Subsections 627.411(1)(b), and 627.412(2), Florida Statutes, expresses general legislative intent and does not provide the Department with specific powers, functions, or duties upon which it may lawfully promulgate a rule that would prevent insurers from excluding or limiting mold coverage; (c) The unadopted rule enlarges the rights of policyholders by mandating coverage for mold as part of the insurers comprehensive policies to the extent that the policyholders have enjoyed such coverage in the past; and (d) The policy gives the Department unlimited discretion to define

"comprehensive coverage" to include any coverage it believes to be "comprehensive," including mold coverage.

49. The Department admits it does not have authority to disapprove an endorsement simply because it seeks to limit or exclude coverage related to mold. Despite this admission, the Department's policy makes mold coverage irrevocable. Such a policy is clearly erroneous because insurers are generally permitted to provide whatever contractual provisions they determine are appropriate, subject to specific statutory and rule limitations. Section 627.414, Florida Statutes, states as follows in relevant part:

> 627.414 Additional policy contents.--A policy may contain additional provisions not inconsistent with this code and which are:
>
> * * *
>
> (3) Desired by the insurer and neither prohibited by law nor in conflict with any provisions required to be included therein.

In this instance, the Department is mandating coverage that is not specifically required by statute or rule.

RECOMMENDATION

Based on the foregoing Findings of Fact and conclusions of Law, it is

RECOMMENDED that the Department enter a final order approving the endorsements filed with the Department by State Farm on November 15, 2001.

DONE AND ENTERED this 5th day of June, 2003, in Tallahassee, Leon County, Florida.

____

WILLIAM R. CAVE
Administrative Law Judge
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Filed with the Clerk of the
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this 5th day of June, 2003.

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NOTICE OF RIGHT TO SUBMIT EXCEPTIONS

All parties have the right to submit written exceptions within 15 days from the date of this Recommended Order. Any exceptions to this Recommended Order should be filed with the agency that will issue the Final Order in this case.