

## DEFECTIVE BUILDING EXTERIORS: HARDBOARD SIDING AND EXTERIOR INSULATION AND FINISH SYSTEMS (“EIFS”)

In recent years, homeowners have experienced large-scale failures and problems with two popular types of home exterior products: hardboard siding and EIFS (more commonly referred to as “synthetic stucco”). There have been several national class action lawsuits against the manufacturers of these building products. From a REALTOR’S® perspective, the problems with these materials on homes present new disclosure issues.

### I. FACTUAL BACKGROUND

#### A. The Product

##### 1. Hardboard Siding

Hardboard siding is a catch-all term for various types of composite wood siding designed to look like solid wood planks. According to industry information, these products are made from wafers of wood that are coated in resin, and then formed into “mats.” These products are realistic wood substitutes and are often difficult to distinguish from wood. Major national manufacturers of hardboard siding include Louisiana-Pacific (“LP”), ABTCO/Abitibi, Masonite Corporation, Georgia-Pacific, Boise Cascade Corporation and Weyerhaeuser.

##### 2. EIFS

EIFS, a stucco-like exterior finish, was originally developed in Europe after World War II to cover masonry, brick and stone damaged during the war.<sup>1</sup> EIFS systems consist of a thin, cement-like base coat applied directly to exterior sheathing, attached to a foam insulation board.

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<sup>1</sup> Carroll, Bill, Synthetic Stucco: All It’s Cracked Up to Be?, Tar Heel REALTOR® (North Carolina Association of REALTORS®, May, 1998).

EIFS became attractive to U.S. builders during the 1970's energy crisis, as its foam core and impervious exterior finish makes an excellent overall insulation blanket for homes. Also, EIFS never needs painting, and its flexibility allows architects to design details (such as cornices and arches) which would be prohibitively expensive using conventional construction methods.<sup>2</sup> Leading manufacturers of EIFS products include Dryvit Systems, Inc., Parex, Inc., Senergy, Inc., STO Industries, and Simplex Products of Adrian, Michigan.

## **B. The Problems**

### **1. Hardboard Siding Failures**

Problems with hardboard siding appear in several ways, including warping, buckling, mold growth and the separation of the siding's outer covering from its pressed wood inner core. These problems do not appear to be limited to any particular climate or geographical location, but have occurred on a nationwide basis. At least one manufacturer, LP, has stopped producing the suspect siding, which was marketed and installed, generally on new residences, between 1985 and 1996.<sup>3</sup>

### **2. EIFS Failures**

The waterproof exterior surface of EIFS, which acts as a moisture barrier, has ironically become its Achilles' heel.<sup>4</sup> In cases where water is able to penetrate behind the exterior of an EIFS installation, any water which does manage to penetrate the EIFS becomes

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<sup>2</sup> Synthetic Stucco Facts and Fiction, posted on [www.americas-real-estate.com](http://www.americas-real-estate.com) ("America's Virtual Real Estate Store"), at 3.

<sup>3</sup> Special Legal Update: Louisiana Pacific Siding, Indiana REALTOR® Magazine (September, 1998).

<sup>4</sup> Epstein, Steven, Synthetic Stucco Suits Swarm Southeast And Spread, American Bar Association BRIEF (Winter, 2000) at 1.

trapped behind the EIFS barrier and cannot escape. This trapped moisture can cause mold growth and can contribute to rotting of sheathing, framing, sill plates and other wooden structural elements. This damage often remains hidden behind the exterior surface.

### **C. Testing and Remediation**

The problems experienced by hardboard siding owners have, in general, consisted of a complete failure of the product, requiring the removal and replacement of the hardboard siding. The difficulty for hardboard siding owners is identifying the siding's manufacturer, so that claims for compensation can be made against the correct one of several national class action settlement funds.

With respect to EIFS, considerable debate exists in the building and insurance industries as to both the testing and remediation of alleged defects in EIFS-finished homes. EIFS manufacturers often blame problems on faulty installation, including missing or inadequate sealants and flashing, and claim that wholesale EIFS removal is unwarranted.<sup>5</sup> Many consumers concerned about resale and damage to property value have entirely stripped EIFS from their homes, and sought insurance coverage under homeowners' policies to do so. In turn, homeowners' insurers have generally refused EIFS claims under construction-defect exclusions.

The testing process itself is also problematic. In many cases, intact and like-new EIFS exteriors have been found to harbor significant decay and mold underneath. Accordingly, recommended EIFS testing is invasive in nature and requires the use of probes

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<sup>5</sup> For the industry's position, see articles and press releases posted at [www.eifsfacts.com](http://www.eifsfacts.com). Angry EIFS homeowners have posted a rebuttal website at [www.eifsfacts.org](http://www.eifsfacts.org) ("The Real Facts About EIFS").

inserted into holes bored into the exterior cladding to evaluate the moisture content and damage.<sup>6</sup>

## II. LITIGATION AND RISK MANAGEMENT

### A. Hardboard Siding Litigation

Problems with hardboard siding, such as buckling, warping, and swelling, have been known since at least the late 1970's, leading to successful recoveries by individual property owners against hardboard siding manufacturers. By the 1990's, major class action lawsuits had been filed against the leading manufacturers of hardboard siding, including LP, Masonite, Weyerhaeuser, and ABTCO/Abitibi.

National settlements of these class actions have been reached, providing compensation to homeowners who can submit photographs or documentary evidence to establish the presence of hardboard siding on their homes.<sup>7</sup> Typically, the payout from siding manufacturers does not cover the full cost of replacement. Additionally, LP's settlement fund ran out of money recently, leaving 60,000 claims unpaid and prompting a take-it or leave-it offer by LP to settle remaining claims at 35 cents on the dollar.<sup>8</sup> Moreover, the national scope of class action lawsuits has generally barred individual litigation against hardboard siding manufacturers, except by homeowners who timely opted out of the class action settlements. However, these class action settlements with the manufacturers do not preclude

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<sup>6</sup> For Home Owners: If You Have EIFS On Your Home (Washington, DC: National Association of Home Builders, 2001).

<sup>7</sup> See claims procedures detailed on various websites set up to administer the class action settlements, including [www.lpsidingclaims.com](http://www.lpsidingclaims.com), [www.masoniteclaims.com](http://www.masoniteclaims.com), [www.weyerclaims.com](http://www.weyerclaims.com), and [www.abtcoclaims.com](http://www.abtcoclaims.com).

<sup>8</sup> Schmitt, Richard, Plaintiffs See Payouts Shrink in Siding Suit, *The Wall Street Journal* (May 14, 2000).

a homeowner from filing a lawsuit against other parties, such as the builder who incorporated the siding into the home, or against the seller and/or REALTOR<sup>®</sup> involved in the sale and purchase of the home.

## **B. EIFS Litigation**

The EIFS issue first gained national prominence in 1995, when the New Hanover County Inspection Department in Wilmington, North Carolina, began moisture testing of EIFS-clad homes. Inspections conducted found that water had penetrated the sheathing of 71 of 73 homes tested, causing wood so rotten it “would crumble to the touch or peel away like paper.” A March, 1999 Dateline NBC report added to the media furor over EIFS. Many builders stopped using EIFS, and alerted EIFS homeowners of the need for moisture intrusion inspections.<sup>9</sup>

As with hardboard siding homeowners, EIFS homeowners also began filing class action lawsuits across the country. At the time this article was written, there had been only one EIFS class action settlement. EIFS litigation has not been limited to manufacturers, but has expanded to include claims against builders and sellers of EIFS-clad homes. Compensation is often sought for the loss of market value and stigmatization of homes attributed to the presence of EIFS, whether justified or not.<sup>10</sup>

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<sup>9</sup> Synthetic Stucco Suits Swarm Southeast And Spread, *supra* at 2.

<sup>10</sup> Pokela, David, Exterior Insulation and Finishing Systems: The Unfolding Story of the Synthetic Stucco Controversy, at 3 (Greensboro, NC: Adams Kleemeier Hagan Hannah & Fouts, PLLC, July, 1996).

## C. Risk Management

### 1. Hardboard Siding

The issues for REALTORS® in connection with hardboard siding are disclosure issues. Hardboard siding products have clearly been found to be defective, and while a home's hardboard siding might not be in disrepair at the time of sale, a buyer could later be faced with costly repairs.

In fact, a disgruntled buyer has been successful in recovering against a real estate broker in a hardboard siding case. In Thomas v Gray Lumber Company,<sup>11</sup> the West Virginia Supreme Court of Appeals reversed a summary judgment for co-defendant, Patton, Reed & Associates ("Patton, Reed"), a real estate broker. Patton, Reed had dealt with the Thomases, drafting a purchase agreement for their purchase of a new home to be built on a subdivision lot owned by Patton, Reed. Patton, Reed assured the Thomases that the home builder, Colony Construction, "did excellent work, that no problems would arise, and that if any defects became apparent, they would promptly be repaired."<sup>12</sup> Shortly after the Thomases moved in, problems arose, including the home's siding breaking loose and buckling.

While the lower court found that Patton, Reed was not the seller of the home, and thus not liable for its representations, this finding was reversed. In ruling for the Thomases, the Supreme Court concluded that their allegations of misrepresentation were "broad enough to cover parties who may not necessarily have been parties to the sales

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<sup>11</sup> 199 W Va 556; 486 SE2d 142 (1997).

<sup>12</sup> Thomas, 199 W Va at 557-558.

contract.”<sup>13</sup> The Supreme Court commented further that as real estate brokers, Patton, Reed owed a special duty to their customers to detect defects:

[I]t does appear that Patton, Reed & Associates possibly fell into the category of parties who, because of their experience, and because of the nature of their business, generally possessed skill and expertise necessary to make an adequate inspection, and who, in effect, were in a better position to detect defects in workmanship than the ordinary purchaser.<sup>14</sup>

No Michigan case law has imposed a duty upon REALTORS® representing sellers to investigate or discover defects generally, or specifically, the existence of hardboard siding. However, recognizing the risk of lawsuits when hardboard siding fails, the National Association of REALTORS® (“NAR”) has noted that some real estate companies have requested that sellers make voluntary written disclosure as to the presence or condition of hardboard siding, and to have buyers acknowledge receipt of that disclosure.<sup>15</sup> REALTORS® representing buyers should be particularly cautious – while as of yet, there are no Michigan cases delineating the extent of a buyer agent’s duty to discover and disclose any particular kind of defect, the law of agency generally requires an agent to disclose to his client all material information known to the agent which could reasonably affect the client’s decision.

Another disclosure issue arises if the seller has made or settled a claim. According to the terms of the settlement of the class action, claim rights, including the right to

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<sup>13</sup> Thomas, 199 W Va at 561-562.

<sup>14</sup> Thomas, 199 W Va at 561.

<sup>15</sup> Louisiana-Pacific to Replace Defective Exterior Siding, REALTOR® Magazine (August 1, 1997).

receive proceeds, can be transferred between buyers and sellers by the execution of written, notarized “assignment of claim” forms.<sup>16</sup> The terms of these settlements also provide that if a seller has previously been paid by LP for a hardboard siding claim, this fact must be disclosed to a subsequent purchaser. This disclosure is intended to prevent the filing of multiple claims for a single property, for example, in instances where a seller has simply pocketed the claim payment without replacing the hardboard siding. Failure to disclose this fact to a buyer requires the seller to indemnify LP for all duplicate payments made to subsequent purchasers of the same residence.<sup>17</sup> This specific provision of the class action settlement presents a high degree of litigation risk.

## 2. EIFS

Like hardboard siding, EIFS has also mushroomed into a major disclosure issue, requiring expensive and destructive testing. In fact, the National Association of Home Builders now recommends that even EIFS homes undamaged by moisture intrusion be tested at least annually, necessitating additional homeowner expense. Regular monitoring and maintenance of caulk joints is also critical.<sup>18</sup>

Plaintiffs’ lawyers got an early head start in North Carolina, where the EIFS issue first arose, filing one of the first nationwide class actions, Ruff v Parex, Inc. Due to the furor, some North Carolina jurisdictions also banned EIFS in new construction, while others

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<sup>16</sup> See [www.lpsidingclaims.com](http://www.lpsidingclaims.com), “Frequently Asked Questions - Home Sales.”

<sup>17</sup> See [www.americas-real-estate.com](http://www.americas-real-estate.com), “Louisiana-Pacific Inner-Seal Siding,” at 4.

<sup>18</sup> For Home Owners: If You Have EIFS On Your Home, supra at 2.

allowed the use of EIFS only if an internal drainage system were added to allow trapped water to escape (so-called “drainable” EIFS).<sup>19</sup>

Realizing the risk posed to REALTORS<sup>®</sup> by EIFS issues, the North Carolina Real Estate Commission, North Carolina’s licensing agency for real estate professionals, issued a position statement in late 1996 deeming the presence of EIFS a “material fact” and recommending disclosure:

[I]t is the position of the Commission’s legal staff that the presence of synthetic stucco on a property is a material fact and therefore should be disclosed to prospective purchasers. Furthermore, agents should disclose available information about synthetic stucco to consumers and refer them to building inspection offices, manufacturers, and other experts for further information. In addition, agents may wish to refer prospective purchasers to professional inspectors for a thorough examination of the property.<sup>20</sup>

Awareness of EIFS problems quickly spread throughout the country. As the National Association of Home Builders found, while the initial EIFS problem was discovered in and around Wilmington, North Carolina, “field investigations of non-drainable EIFS in other areas of the country have identified entrapped excessive moisture resulting from water intrusion.”<sup>21</sup>

In Schonfeld v Toll Brothers, Inc., a Virginia circuit court allowed plaintiff home buyers’ action to proceed against their buyers’ agent and the listing agent, who had provided

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<sup>19</sup> Exterior Insulation and Finishing Systems: The Unfolding Story of the Synthetic Stucco Controversy, supra at 1.

<sup>20</sup> Kirkman, Dave, Synthetic Stucco Alert, North Carolina Real Estate Commission Bulletin (Winter, 1996) at 2.

<sup>21</sup> For Home Owners: If You Have EIFS On Your Home, supra at 2.

a flyer advertising the home's "stucco" exterior.<sup>22</sup> Approximately two and a half years after purchasing their home, plaintiffs received a letter from co-defendant Toll Brothers, the home's builder, advising them that their home's "stucco" exterior was actually EIFS, not conventional cement-based stucco as plaintiffs had believed.

The court found that the buyers' agent and the listing agent were protected from fraud and non-disclosure claims by Virginia's Residential Property Disclosure Act.<sup>23</sup> While plaintiffs' claims for negligence and breach of fiduciary duty against their buyers' agent were also barred by the statute of limitations, the Court found that on the merits, plaintiffs had stated a cause of action against their buyers' agent for failing to "confirm the authenticity of the information provided about the property."<sup>24</sup>

The real estate industry has responded to the litigation threat by recommending increased disclosure. At NAR's mid-year meetings during summer, 2001, NAR's legal staff took pains to warn brokers about the dangers posed by EIFS litigation, in which brokers were increasingly being named as defendants. NAR noted that approximately 30 states had already amended required sellers' disclosures to include EIFS, and that in the remaining states, many brokers have begun using their own voluntary property disclosure forms.<sup>25</sup>

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<sup>22</sup> Schonfeld v Toll Brothers, Inc., unpublished opinion of the Circuit Court of Virginia, decided November 23, 1999 (Docket No. 182698).

<sup>23</sup> Schonfeld, *supra* at 1.

<sup>24</sup> Schonfeld, *supra* at 2.

<sup>25</sup> Clairmont, Julie, A Stucco Nightmare: Brokers Warned About High Incidence of EIFS-Related Buyer Lawsuits, Inman News Features (July 18, 2001).

At the present time, Michigan's statutory sellers' disclosure form does not include a specific EIFS disclosure.<sup>26</sup> EIFS litigation has reached Michigan, however, and the Michigan Court of Appeals recently allowed a homeowner's EIFS product liability claim to proceed against Michigan-based EIFS manufacturer Simplex Products Division/K2, Inc. In that case, plaintiff alleged mold and structural damage caused by the application of EIFS. Simplex Products successfully contended that plaintiff's action was barred by various UCC provisions, but the Court of Appeals reversed this finding.<sup>27</sup> It may be only a matter of time before Michigan plaintiffs institute actions against REALTORS® involved in the purchase and sale of EIFS-clad homes, especially since the cost of stripping and recovering a home with alternative materials can exceed the original cost of the EIFS installation.

In summary, the risk of litigation only may compel sellers' agents to voluntarily recommend disclosure of residential EIFS. Again, buyers' agents need to be particularly cautious, as one day, a purchaser will certainly assert that their agent knew or should have known of this defect and disclosed that information to his client. Buyers' agents should be aware that the recommendation of a home inspection by a competent home inspector may not be enough. EIFS homeowners have found that even certified home inspectors (e.g., with certification through ASHI, the American Society of Home Inspectors) have often missed moisture problems with EIFS exteriors. Buyers' agents should be aware that conventional home inspections may not be sufficient to serve buyers' needs in an EIFS-clad home transaction.

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<sup>26</sup> MCL 565.957; MSA 26.1286(57).

<sup>27</sup> Blackward v Simplex Products Division, unpublished opinion of the Court of Appeals, decided October 19, 2001 (Docket No. 221066).

### III. REGULATORY RESPONSE AND LEGISLATION

As mentioned above, in response to the hardboard siding and EIFS controversies, many states have amended seller's disclosure laws to require disclosure of the presence of these items. North Carolina, for example, has merely added check-offs for composition/ hardboard siding and synthetic stucco.<sup>28</sup> Other states have opted for greater detail, such as Tennessee, whose EIFS disclosure provides:

21. Any exterior wall covering of the structure(s) covered with exterior insulation and finish systems (EIFS), also known as "synthetic stucco"?

YES NO UNKNOWN

If yes, has there been a recent inspection to determine whether the structure has excessive moisture accumulation and/or moisture related damage? (The Tennessee Real Estate Commission urges any buyer or seller who encounters this product to have a qualified professional inspect the structure in question for the preceding concern and provide a written report of the professional's finding).

YES NO UNKNOWN

If yes, please explain. If necessary, please attach an additional sheet.<sup>29</sup>

In addition to requiring seller disclosure, many jurisdictions have amended building codes to prohibit the use of EIFS for new residential construction. North Carolina,

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<sup>28</sup> See NCGSA § 47E-4, Residential Property Disclosure Act, and amended disclosure form, NC Admin Code, title 21, R 58A.0114.

<sup>29</sup> TCA § 66-5-210.

where awareness of EIFS problems first arose, subsequently banned the use of EIFS, followed by Georgia.<sup>30</sup> Other jurisdictions have amended building codes to allow only the use of EIFS which is “drainable,” or “water-managed,” including a moisture barrier protecting water-sensitive materials behind the EIFS and drains to allow moisture to escape. Michigan falls into this latter category by its adoption of the International Residential Building Code during 2001, which requires the above cited measures in EIFS installations.<sup>31</sup> Nevertheless, enough conventional EIFS installations were made prior to building code changes to ensure that disclosure will remain a future concern for buyers, sellers and REALTORS®. Even “drainable” EIFS, the current alternative, has not been around long enough to prove itself, according to building industry sources.<sup>32</sup> While this debate continues, litigation can certainly be expected to continue as well.

#### IV. CONCLUSION

From all accounts, the current furor over hardboard siding and EIFS shows no sign of abating. Numerous class actions remain pending, seeking nationwide class certification, and several lawsuits by homeowners and home buyers in other states have already succeeded in imposing liability against various parties in addition to the manufacturers of these products.

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<sup>30</sup> Baylis, Jamie, Filing Deadlines Near in Synthetic Stucco Cases, The Washington Post (March 31, 2001) at H01.

<sup>31</sup> Martin, R. Thomas, Director, Michigan Office of Policy and Legislative Affairs, in correspondence to Michigan 2<sup>nd</sup> District Sen. William Van Regenmorter, June 5, 2000 (posted at [www.eifsfacts.org/michigan.htm](http://www.eifsfacts.org/michigan.htm)).

<sup>32</sup> Filing Deadlines Near in Synthetic Stucco Cases, *supra* at 6.

In the absence of legislation, the law on disclosure as to hardboard siding and EIFS is the same as the law on disclosure as to any other potential defect in a home. REALTORS® should keep in mind, however, that the cost of replacing these products and the damage caused by these products can be significant. Accordingly, REALTORS® who represent sellers of homes with these products should strongly recommend to their clients that they make appropriate disclosures. REALTORS® representing potential buyers of homes with these products should advise their buyer clients of possible problems with these types of products and refer these buyers to appropriate professionals to evaluate the situation.

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