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Let's be honest. How many of us really read the insurance section of a lease? Now let's be really, really honest: Who understands what that section means?

Commercial general liability (CGL) insurance versus property and casualty insurance. Named insureds versus additional insureds. Waivers of subrogation, etc., etc.

All of this ignorance is bliss just so long as no one gets hurt and nothing gets damaged. Then all of that ignorance turns into: We have no insurance for that?! And, You mean I have to pay for that?

The painful truth is you can't and shouldn't own, lease, or manage real estate unless you know the basic types of property-related insurance, important terminology and provisions, and the special insurance concerns that affect the parties to a lease.

First, know the types of insurance associated with real estate-related risks. The two most common of these policies are casualty and liability insurance.

MOTHER NATURE AND MORE

Casualty insurance, also referred to as property insurance or property and casualty insurance, provides coverage for fires, storms, and other causes of physical damage to buildings and improvements. Typically, the landlord will provide casualty insurance for the building structure, including roof, walls, and floors, as well as common area improvements. The tenant will typically provide casualty insurance for the tenant's improvements to its premises, as well as the tenant's personal property within the premises.

In some leases, such as ground leases and leases of free-standing buildings, the tenant will procure the casualty policy for the building and all of the improvements and personal property, and even where the casualty insurance on the building is procured by the landlord, some or all of the cost of the insurance is typically borne by the tenants.

Liability insurance, often referred to as commercial general liability insurance, provides coverage for slips and falls and other injuries in and about the insured property. Usually, the tenant will procure liability insurance with respect to occurrences in and about the tenant's premises. The landlord will procure a separate policy with greater insurance coverage for the entire property. Again, some or all of this insurance cost is almost always passed on to the tenants.



BUSINESS INTERRUPTION

Insurance is also available and often procured for economic losses due to the inability to use real estate.

The tenant's commercial general liability policy will usually include business interruption insurance, which provides compensation for overhead that must be paid and/or revenue that is lost when

the tenant's premises cannot be used due to power outages, casualties, and other causes. Similarly, a landlord CGL policy might include rent loss insurance, which will replace some or all of the rent that is not paid by tenants that cannot use their premises because of a casualty.

Other applicable insurance policies include workers compensation insurance, which provides compensation for employees injured on the job; boiler and machinery insurance, which provides insurance for damage caused by heavy machinery, especially machinery that is susceptible to explosions; and environmental or pollution insurance, which provides coverage for remediation and other costs associated with the discharge of hazardous substances.

KNOW THE LANGUAGE

Second, understand the key provisions and terms. For example, each party to a lease should understand and procure a waiver of subrogation provision from the other party's property insurer. In short, when an insurance company insures property and pays a covered claim with respect to that property, the insurer steps into the shoes of the owner of that

property by the process of subrogation and may recover the amount paid on the claim from the party that damaged the property.

For example, if you are the tenant and you leave a coffee pot on and burn down your landlord's building, the landlord's insurance company may pay the landlord for the damage to the building and then sue you to recover the amount paid. By paying the claim to the landlord, the insurance company is entitled, by subrogation, to the landlord's right to sue you for the damage to the landlord's property.

Accordingly, each party to a lease should insist on procuring a waiver of subrogation from the other party's property insurer. It is important to note that the insurance company still gets to keep all of the insurance premiums that the landlord has been paying, so any recovery by subrogation is a windfall to the insurance company (and if an insurance company won't provide the waiver, get another insurance company).

Key terminology includes the distinction between additional insured and named insured. An additional insured is afforded coverage by the insurance policy but does not control the policy. A named insured is not only covered by the policy but also controls the policy and generally has the right to approve the settlement of claims. Similarly, a loss payee is the party to whom the insurance company will disburse insurance proceeds when a claim is paid.

Also, insurance procured in connection with leases generally provides coverage on an occurrence basis; that is, if the covered claim occurred during the term of the insurance policy, then the claim can be submitted later and will within certain limits be paid after the term of the insurance policy expires.

PAY SPECIAL ATTENTION

Insurance for professional services (such as the design

services of an architect) is covered on a claims made basis. Under this type of insurance, the policy must be in effect when the claim is submitted. Here, great care is necessary in drafting the appropriate requirement to maintain the claims made policy for as long as a legitimate claim may be submitted.

Be aware of special concerns. For example, when insuring buildings, a special ordinance or law rider may be needed to ensure that the policy will pay for improvements, such as a sprinkler system, that may not have been required when the building was built, but might be required to rebuild in accordance with new requirements.

EXTRA CONSIDERATION

Similarly, certain specific insurance requires careful review: Environmental or pollution insurance frequently includes significant limitations which may well defeat the purpose of procuring the insurance. In other cases, you may be unaware of the need for a special insurance coverage, such as insurance for an off-property power failure that prevents you from using your property. In addition, you must coordinate your insurance coverage with the related provisions of your lease.

For example, business interruption insurance often is limited to 12 months of overhead and rent replacement, so the tenant should be entitled to terminate its lease if the premises cannot be reoccupied within that time period. Other special concerns include obtaining the appropriate replacement cost coverage, avoiding co-insurance requirements, and protecting against undervaluation of your property or your possible rent loss.

With an understanding of the insurance basics, as well as the assistance of a skilled insurance adviser and sound legal guidance, your insurance plan can be more than just hoping for the best.

ABOUT JACK GARSON



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Jack Garson's practice focuses on Real Estate, Construction and Business law. He serves as a legal advisor for numerous local, regional and national companies. In his role as legal counsel, Jack also serves as a strategic advisor and lead negotiator. Further, Jack provides guidance on the structure of complex transactions, the resolution of business disputes, the growth and sale of companies, and the management of issues such as liability and risk reduction, employment practices, and enhancing profitability.

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