



Risks in Property and Casualty Insurance Every Real Estate Lawyer Should Know

ACRELive – September 26, 2019

Charles Comiskey
President, Risk Tech, Inc.
Houston, Texas

John McNearney
Polsinelli PC
St. Louis, Missouri

Property & Casualty Insurance

- Property Insurance
 - 1st party – reimburses insured for its own “covered causes of loss”
 - Can include loss of income, flood, quake, terrorism
 - Contingent property insurance – provides coverage when primary insurance doesn’t (e.g. – triple net tenant coverage lapse)
- Casualty Insurance
 - a/k/a Liability Insurance
 - 3rd party – pays amounts the insured owes to someone else

ISO vs. Manuscript

© Insurance Services Office, Inc. (ISO) – collects data, promulgates ratings, develops forms and files information with state regulators

© ISO Properties, Inc., 20__

- Widely recognized industry standard coverage forms
- Substantial case law
- Issued numerous endorsements with 12 19 dates

ISO vs. Manuscript

- Manuscript Policies – are customized
 - “Includes Copyrighted Material of ISO With Its Permission”; or
 - Makes no reference to ISO
 - Non-standard
 - Little to no case law
 - Here’s your sign

ISO Property Insurance Forms

- Basic Causes of Loss CP 10 10
 - “Named causes of loss” form
 - Covers eleven listed risks
- Broad Causes of Loss CP 10 20
 - “Named causes of loss” form that covers the same perils plus additional causes – falling objects, weight of snow, ice or sleet and water damage
- Special Causes of Loss CP 10 30
 - Covers all risk of direct physical loss unless specifically excluded
 - Still must endorse if want flood, earthquake, volcanic action, terrorism, equipment breakdown

Covered Amount

- Actual Cash Value (ACV)
 - Replacement cost less depreciation
- Replacement Cost (reconstruction)
 - @ original location
 - ACV paid until restoration is performed
 - What if lender won't allow use of insurance to rebuild?



Debris Removal

- Commonly 25% of the amount of direct physical loss
- Within the covered limit (erodes that limit)
- Additional amount may be available but ...



Ordinance or Law

- Value of Loss of Undamaged Portion of Building which must be demolished
- Demolition Cost
- Increased Cost of Construction



Coinsurance

- Warranty to the insurance company
- Minimum of 80% for specific structure
- Minimum of 90% for blanket coverage
- Coinsurance Penalty applies for noncompliance (under-insuring)



Coinsurance Penalty

- Assume reconstruction cost of \$1,000,000 on specific structure subject to an 80% coinsurance clause and \$250,000 loss occurs
- $\$1,000,000 \times 80\% = \$800,000$ minimum limit required
- Insured procures only \$500,000 limit
- $\$500,000 / \$800,000 = .625 \times \$250,000 =$ loss payment of \$156,250 less deductible
- \$93,750 difference is the coinsurance penalty

Blanket Coverage

- Assume 3 buildings with reconstruction costs of \$2,000,000, \$3,000,000 and \$5,000,000, insured on a blanket basis subject to a 90% coinsurance clause
- $\$10,000,000 \times 90\% = \$9,000,000$ minimum limit required
- Insured procures \$9,000,000 limit
- Building #2 burns & reconstruction cost turns out to be \$3,500,000
- Full blanket limit is available – insured recovers \$3,500,000 so long as overall coinsurance requirement has been met or Agreed Value coverage provided

Valuation Endorsements

- Agreed Value – eliminates the possibility of a coinsurance penalty for that policy
- Margin Clause – eliminates the advantage of blanket insurance
 - Ranges from 1.00 to 1.30 of specific declared limit
 - Using blanket example and 1.10 margin clause, insured would recover only \$3,300,000 - \$200,000 less
 - Consider prohibiting

Income Coverages

- Business Income
 - Restaurant or manufacturing plant example
 - Net income + continuing normal operating expenses
- Extra Expense
 - Law firm example
 - Extraordinary additional expenses not normally incurred
- Loss of Rental Value
 - Apartment project example
 - Fair rental value less operating cost
- Coinsurance may apply.
- Mortgagee shall be named as additional insured on CP 15 03.

Vacancy

Vacancy compromises coverage. In a commercial property policy, vacancy is defined as:

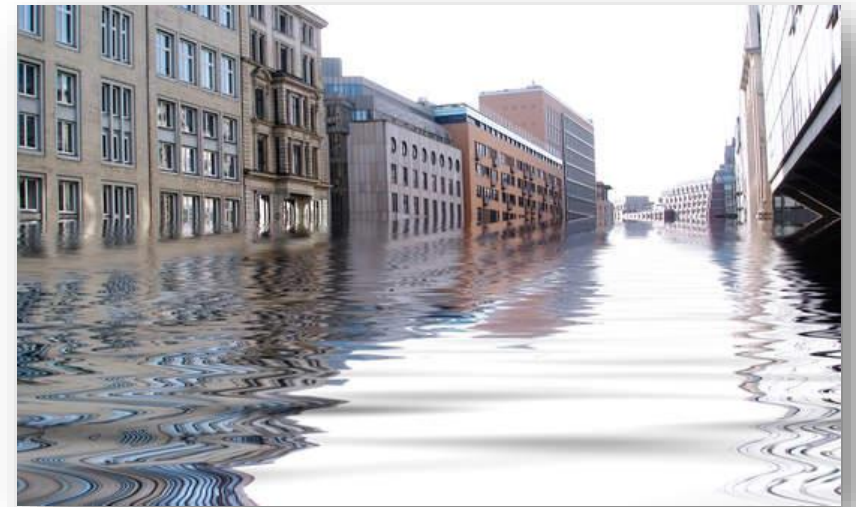
- When this policy is issued to a tenant, and with respect to that tenant's interest in Covered Property, building means the unit or suite rented or leased to the tenant. Such building is vacant when it does not contain enough business personal property to conduct customary operations.
- **When policy issued to owner/general lessee of a building, building means the entire building. Such building is vacant unless at least 31% of its total sq. footage is:**
 - **Rented to lessee/sub-lessee and used by lessee/sub-lessee to conduct its customary operations; and/or**
 - **Used by building owner to conduct customary operations**

Vacancy for a period of more than 60 consecutive days voids coverage for losses arising from vandalism, sprinkler leakage (unless the system has been protected against freezing), water damage, building glass breakage, theft, and attempted theft. Recovery for any other covered cause of loss is reduced by 15%. The building must have been vacant at the time of loss and for the 60 preceding days for this coverage restriction to apply.

Flood Insurance

Problem #1: Public Perception

- “My mortgage company said I didn’t need flood insurance.”
- “I don’t need flood insurance. I’m not in a flood zone”.
- “We’ve owned this property for 75 years and it’s never come close to flooding.”
- “I have the max sold by NFIP. That’s enough.”
- “What? Flood isn’t covered by my insurance?”



Flood Insurance

Problem #2: Actual Experience

- Harvey damaged more than 200,000 homes, 75% of which were outside of the 100 flood plain
- Flood maps guide key development decisions but 30% of damaged homes outside of 100 flood plain had water up to waist of homeowners
- Houston has had two 500 year and one 1000 year flood in past three years
- Flood zones continue to be used but are old science
 - No flood zone is safe



Flood Insurance

Problem #3: NFIP Coverage

Advantages:

- Available community wide
 - Even if in high-risk area
 - Even if insured has prior loss experience
- Reasonably priced
- Low deductibles

Disadvantages:

- Limited amount of coverage
- Limited scope of coverage for damaged property
- No coverage for business income/loss of rents/additional living expense



Privatization

- Difference in Conditions (“DIC”)
- Computing power: Big Data
- Coverage limits and rates that are more favorable than NFIP
 - Fewer requirements
 - Immediate binding
 - Improved definitions
 - Higher limits
 - Broader coverage:
 - Replacement cost
 - Business Income

Parametric Insurance

- Not based on damage incurred like traditional insurance
- Based on data triggers
 - Wind velocity
 - Water height
 - Tax revenue shortfall
 - Circumstances that harm the economy
- Data comes from third party agreed upon by stakeholders

Self-Insurance

- Self-insurance = no insurance
- None of the insurance requirements apply
- Take care to contractually require that self-insured exposures be treated as though fully insured

Mortgage Holder, Lender Loss Payable, and Loss Payable Clauses

- **Mortgagee Clause:**
 - Includes protection against policy being invalidated by action of insured.
 - Notice of cancellation provided.
 - Claim payment to be made to lender and insured jointly.
- **Lender's Loss Payable Clause:**
 - Includes protection against policy being invalidated by action of insured.
 - Notice of cancellation and nonrenewal is provided.
 - Fails to discuss handling of claim payment.
- **Loss Payable Clause:**
 - Geared to machinery & equipment.
 - No protection against invalidation.
 - No notice of cancellation.

General Liability Insurance

- Limits of Liability
 - Per Occurrence
 - General Aggregate
 - Products/Completed Operations Aggregate
- Designated Location(s) General Aggregate Limit

Additional Insured

- CG 20 18 04 13 - Additional Insured - Mortgagee, Assignee or Receiver
- Only with respect to liability as mortgagee, assignee or receiver and arising out of the ownership, maintenance or use of the premises by the primary insured
- Excludes structural alterations, new construction and demolition operations

Primary and Non-Contributory Liability

- CG 20 01 04 13
- This insurance is primary to and will not seek contribution from any other insurance available to an additional insured under your policy provided that:
 - The additional insured is a Named Insured under such other insurance; and
 - You have agreed in writing in a contract or agreement that this insurance would be primary and would not seek contribution from any other insurance available to the additional insured

Waiver

- Waiver of Subrogation
- Waiver of Right of Recovery

Prohibited Exclusions and Limitations

- Amendment of Insured Contract Definition CG 24 26
- Classification or Business Description
- Contractual Liability Limitation CG 21 39
- Insured vs. Insured
- Limitation of Coverage to Designated Premises or Project CG 21 44
- Punitive, Exemplary or Multiplied Damages

Other Liability Coverages

- Auto
- Workers' Compensation
- Liquor
- Excess
- Pollution (mold)
- Terrorism

Certificates of Insurance

“It is a tale, told by an idiot, full of
sound and fury, signifying nothing.”
- Macbeth

Certificate Specifications

- ACORD 25, Certificate of Liability Insurance
- ACORD 28, Evidence of Commercial Property Insurance
- Both are replete with disclaimers and are generally held to be unenforceable against the insurance companies designated on the certificates.
- Detailed certificate requirements should be included in any contract, the intent being to get the other side's insurance agent to state what coverage is not being provided. See paper.

Certificate Specifications

- Require form giving notice of cancellation
- Require borrower to provide original policy
- Obtain copy of at least declarations page and Schedule of Forms and Endorsements page(s)
- Ask about forms that you do not recognize
- Assure that lender is named as lender loss payee or mortgagee

Questions

Charles E. Comiskey


Charles.comiskey@risktechinc.com

713.254.1818

John McNearney

JMcNearney@polsinelli.com

314.622.6171



Polsinelli PC provides this material for informational purposes only. The material provided herein is general and is not intended to be legal advice. Nothing herein should be relied upon or used without consulting a lawyer to consider your specific circumstances, possible changes to applicable laws, rules and regulations and other legal issues. Receipt of this material does not establish an attorney-client relationship.

Polsinelli is very proud of the results we obtain for our clients, but you should know that past results do not guarantee future results; that every case is different and must be judged on its own merits; and that the choice of a lawyer is an important decision and should not be based solely upon advertisements.

© 2019 Polsinelli® is a registered trademark of Polsinelli PC. In California, Polsinelli LLP. Polsinelli PC (Inc) in Florida.



polsinelli.com