WHAT EVERY LEASING ATTORNEY NEEDS TO KNOW ABOUT INSURANCE:

ASK FOR WHAT YOU WANT. THEN MAKE SURE THE INSURANCE COVERS WHAT YOU NEED

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by Angelia D. Wesch, Member
and Carmen R. Rowe, Associate
Eisenhower & Carlson PLLC Real Estate and Land Use Group

Eisenhower & Carlson PLLC
Wells Fargo Plaza, Suite 1200
Tacoma, Washington 98402
(253) 572-4500
awesch@eisenhowerlaw.com

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Every leasing attorney needs to be cognizant of the insurance issues swirling around the landlord-tenant relationship they are creating. Thoughtful consideration of the influence of insurance on the landlord-tenant relationship is particularly critical in the commercial context. Insurance is the elephant in the room that cannot be ignored.

The lease will determine how the parties' liabilities are allocated. Insurance determines how the parties will pay for those liabilities, and just as (if not more) importantly, how the parties will pay the legal costs of handling claims. A well drafted lease will blend these two considerations into a cohesive whole, ensuring that the parties' respective liabilities are backed by insurance to the fullest degree possible.

The prudent lease lawyer remains ever mindful of case law and recent litigation trends. All good lawyers know that awareness of how leases can go wrong helps them draft a sound lease that minimizes the chances for litigation to begin with, and, if litigation should occur, optimize the client's chances for success in recovering for unexpected losses. Awareness of the insurance component, how the courts will assess the parties' insurance obligations under the lease, and how insurance will influence the leasing parties' respective rights should something go wrong, will further facilitate a sound lease upon which your clients can rely.

GETTING THE BASICS: THE ROLE OF PROPERTY AND CASUALTY INSURANCE IN REAL ESTATE

In their most basic forms, property insurance and casualty insurance are just what they sound like. However, leases often incorrectly reference property insurance when what is really intended is liability (casualty) insurance. It is important to recognize the distinct nature of the two types of insurance so that the lease may address both types comprehensively.

Property insurance helps to cover losses to real and personal property owned by either the landlord or tenant. The application of property insurance to lease relationships is an intuitive one: insurance to cover damage to the real property that is the subject of the lease and personal property on that land.

The important distinction is that such insurance only covers direct losses of property owned by (or otherwise under possession of, as defined specifically in the policy) *the insured*. Therefore, it is critical that any insurance policy encompasses the intended property as "your" property, or otherwise fits a policy definition of covered property.

Casualty insurance fills the gap to cover liabilities other than direct damage to the property of the insured, including bodily injury, damage to business, and damage to property of third-parties. The application of casualty insurance to leases should be obvious to the experienced practitioner. For example, casualty insurance covers claims for personal injury that occurs on the property. Of particular importance in the scope of commercial leases, this type of insurance also covers the interruption of business. This may include loss of business opportunity during course of repair after an emergency or other property damage, or expenses associated with operation off-site during any lengthy repair. It may also include losses incurred due to interruption of utility services caused by repair, construction or disaster.

Similar to property insurance, the real trick in casualty coverage is to ensure that the person bearing the responsibility for a particular loss is also the insured for that loss. In property insurance matters you want to be sure that the property you intend to protect is considered the property of the insured, or is otherwise covered by the insured's property coverage. In casualty insurance you want to be sure that the insured is the person responsible for the loss. To accomplish this, the savvy drafter will ensure that the lease clearly identifies the losses to be covered by any required insurance, and that the person required to obtain coverage for specific losses is the same person identified in the lease as the one responsible for those losses.

For both property insurance and casualty insurance covering liabilities relating to the property, there may be coverage problems relating to the question of ownership for any given real or personal property on the leased property. One way to minimize such problems is to ensure that both tenant and landlord are considered insureds. The most common way this is accomplished is to require that the landlord is listed as an additional insured (casualty coverage) or loss payee (property coverage) under any policy that the tenant is required to carry. The lease should also require that at the outset of every policy year of coverage, the insuring party provide sufficient proof of insurance (not just a certificate of insurance, but also a declarations page and any endorsements, and even a copy of the policy) affirming the other party's status as an insured.

> ***Practice tip:*** As obvious as it may sound, it is imperative that any party expecting coverage as an additional insured or loss payee confirm that such coverage and designation was in fact put into place. Too often, in leasing situations as with many others, a party will require that the other procure coverage and list them as an additional insured or loss payee, but never follow up to ensure that they actually received proof of such coverage and complete copies of the policies, including all endorsements, from the procuring party or its insurance broker affirming they were properly named in the policy. At the outset of the relationship this little detail is often neglected in the flurry of paperwork typically flying back and forth. Oversights happen, whether because proof of insurance was never provided or because the policy failed to name the proper party as an additional insured or loss payee. A party may also neglect to ensure receipt of the appropriate proof of insurance in subsequent policy years. This seemingly minor administrative oversight can rapidly evolve into a problem of monstrous proportions should a dispute later arise and an

omission of the intended additional insured or loss payee preclude or impair coverage for the loss. It is also critical to obtain the necessary proof as a potential condition precedent where the lease requires such documentation before the lease commences.[1]

Practice tip: Whether named as either an additional insured or loss payee, it is prudent to consider the effect that any subrogation clauses (or wavier of such rights) in the lease may have on the parties' status as an additional insured or loss payee.[2] It is impossible to generalize as each lease will contain a different balance of liabilities. But careful consideration of the insurance company's subrogation rights under the policy as they relate to the parties' obligations under the lease, and the parties' respective relationship to the policy (for example, whether the party is an additional insured or not), will help prevent unpleasant surprises down the road.

APPLYING INSURANCE TO LEASING OBLIGATIONS: SOME SPECIFIC AREAS OF CONCERN

The sections below outline some common issues to consider when identifying the required property and casualty coverages and – critically – when reviewing policies to ensure the coverage is adequate and compliant with the lease. The below examples illustrate some of the myriad ways insurance coverage issues that crop up in litigation intertwine with leasing obligations. These types of issues must be considered both when allocating responsibilities in the lease, and in ensuring that those losses are covered by insurance to the fullest extent possible. The sections below will address the following:

- Concerns particular to property coverage.
- Concerns particular to casualty coverage.
- Concerns that affect both property and casualty coverage.

Concerns Particular to Property Coverage.

Property coverage deals with losses to any real or personal property of the insured, be that the landlord or tenant. Ensuring appropriate property coverage – including making sure that any policy in place actually covers the desired property – helps protect the investment of both landlord and tenant. It also minimizes the chances that the landlord and tenant will have to resort to suing each other to recover from potentially substantial losses.

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[1] *See, e.g., Woody's Steaks, LLC v. Pastoria*, 584 S.E.2d 41 (Ga.App. 2003)(lease requirement that tenant maintain liability insurance constitutes a condition precedent, where lease required tenant to provide proof of insurance before commencement of lease).

[2] For more discussion on this issue, see Ann Peldo Cargile's article Digging Into Ground Leases: Insurance and Reconstruction Issues, ABA's Probate & Property March/April 2006 issue at 42, 45.

SCOPE OF REPLACEMENT COST.

In a commercial context it is particularly important both landlord and tenant ensure that the property coverage will provide actual replacement cost and not just "actual cash value."[3] There are many factors that may render the "actual cash value" substantially less than what is actually needed to put the parties back in the position they were before the loss. The landlord needs to ensure that they regain a useable building, and the tenant needs to ensure that they receive the equipment needed to continue their operations as seamlessly as possible.

EFFECT OF UPDATED CODE REQUIREMENTS.

Several property coverage policies include exclusions for the added costs of re-building incurred because of new code or other government requirements. A well drafted lease will make it clear who is the responsible party for such costs, and will address whether or not additional insurance is required to cover such costs. If such losses are to be self-insured, the other party's advisor should recommend that there is some security in place to ensure that the responsible party is actually able to pay should the need arise. All too often, the costs of upgrading new construction to comply with increasingly stringent building or other local codes and regulations can rapidly outpace the costs of simply rebuilding what was there.

Concerns Particular to Casualty Coverage.

Concerns relating to casualty coverage include the following common examples:

IMPOSSIBILITY.

The parties should address in their lease what will happen should the building prove to be impossible to rebuild in the event of severe damage, such as where there are new government restrictions (such as proximity to a shoreline or wetland) or where replacing the building or damaged components proves economically impractical.[4] Impossibility will typically relieve the parties from their respective obligations, which leaves both parties in a potential lurch.[5] Such situations may be addressed in the lease in a manner similar to a condemnation or

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[3] For an excellent discussion on the need to carry full replacement cost and avoid the risks of coinsurance, see Cargile, Digging Into Ground Leases: Insurance and Reconstruction Issues, ABA's Probate & Property March/April 2006 issue at 42.

[4] Impossibility or frustration of purpose will excuse performance because the value of performance has been destroyed. This doctrine is not limited to strict impossibility, but includes impracticability due to unreasonable expense. *See, e.g., Hopfenspirger v. West*, 949 So. 2d 1050 (Fla.App.5.Dist. 2006).

[5] *See, e.g, In re Dreliouch*, 359 B.R. 9 (Bankr.D.Mass. 2006)(an unexpected event may nullify a contract by impossibility, but only where the event made performance so vitally different from what the parties originally contemplated that the change can be said effectively to have vitiated consent of parties); *see also WRI/Raleigh, L.P. v. Shaikh,* 644 S.E.2d 245 (N.C.App.2007)(under the doctrine of "frustration of purpose, performance may be possible but is excused where a fortuitous event intervenes to cause a

eminent domain. The parties must consider who is responsible for any business losses flowing from the loss of the use of the property, and may want to consider putting appropriate insurance in place to cover such losses.

> ***Practice Tip:*** Typically each party will shoulder the financial responsibility for such a total loss (the landlord bears the loss of the building and the tenant bears the loss of the business), and thus, one might think that it is really just up to each party to procure the requisite coverage for their own losses. However, by ensuring that "the other guy" has appropriate insurance to cover such a loss, the parties do in fact protect themselves as well. Requiring adequate insurance to cover a permanent loss helps minimize the chance that one party finds themselves without adequate coverage, thus facing a substantial and devastating loss for which they may turn to the other party to recover. If there is money to mitigate the loss from insurance, such risks are minimized.

In the event of substantial repairs or a rebuild, the parties may also find that rebuilding to comply with new government requirements creates a situation where the changed components of the new building are no longer conducive to continued operations of the tenancy. This is another form of impossibility or frustration of purpose. The landlord's counsel will want to ensure that the tenant bears full responsibility for any business losses incurred in such an event. For ground leases or other leases that do not allow a tenant to terminate the lease in the event of major damage to the building or facility, the tenant needs to also consider insurance to cover both a new location as well as any continuing lease obligations.[6] Both parties will want to ensure that the tenant has adequate coverage to protect against such a loss. The tenant's interest in such coverage is obvious. For the landlord's part, the landlord will want to be sure the tenant is not left stranded without the financial ability to move on with its business, and thus with incentive to pursue remedies against the landlord for their business losses whether justified under the lease or not.

DELAY AND EFFECT ON BUSINESS OPERATIONS.

In any event where construction may be at issue – whether because the premises is being newly constructed or where substantial repairs are being done – both parties must consider who is responsible for the intangible but critical loss relating to business interruption. The landlord may lose monies in rent for every month tenancy is suspended. The tenant may lose monies and long-term business opportunities for every month they are not operating. The potential variations are too vast to generalize, except to say that both parties must consider the potential ways the tenancy may be interrupted both before the lease commences and later in

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failure of consideration, or a nearly total destruction of the expected value of the performance; though frustration of purpose will not excuse performance when it was foreseeable).

[6] For further discussion on issues peculiar to ground leases, *see* Cargile, Digging Into Ground Leases: Insurance and Reconstruction Issues, ABA Property & Probate March/April 2006 at 42, 43.

the case of repairs or rebuilding. Insurance should be required to cover any such losses, particularly in the case of repairs or rebuilding.

DUTY TO INDEMNIFY VERSUS DUTY TO INSURE.

It is important to note that an agreement to indemnify is separate from an agreement to insure. If one party assumes not only the duty to indemnify the other but also to insure that risk, that party may be in breach of the lease if they fail to procure the requisite insurance even if they do not breach their duty to indemnify.

For example, in the recent Illinois Appellate case Sears. Roebuck & Co. v. Charwil Associates, Ltd. Partnership decided in March 2007,[7] the underlying claim revolved around an injury sustained by a Sears customer in the common area of the mall. The injury was caused by a Sears employee while driving another customer's car. The lease required three distinct obligations: (1) a requirement for the landlord to obtain a commercial general liability policy with certain limits; (2) an agreement that the landlord would indemnify Sears for "any and all" claims arising out of any customer's use of the common areas; and (3) an agreement to provide insurance for, among other things, "insuring the indemnity agreement." The policy the landlord procured had the requisite policy limits, and correctly named the tenant as an additional insured. However, the landlord's commercial general liability policy had an automobile exclusion, and the insurer thus denied coverage for the claim. The landlord also argued that it should not be held liable for the tenant's own negligence.

In the course of litigation Sears asserted claims against the landlord for failure to indemnify and failure to procure the necessary insurance given the insurer's denial of the claim. Sears voluntarily dismissed the claim for failure to indemnify, but pursued its breach of contract claim for failure to procure the required insurance. The court found that even though the landlord did not breach its duty to indemnify, the landlord still breached the lease by failing to procure insurance that met the lease's insurance requirements – e.g., to cover "any and all" claims, which in turn encompassed even those claims caused by a Sears employee. Thus, under the provisions and limitations of that particular lease, the landlord was held liable for the full policy limits of the insurance that was supposed to be in place.

> ***Practice Tip –*** While discussed elsewhere herein, the lesson bears repeating: it is prudent to check to be sure that the coverage procured is the coverage required. The *Sears* case is a good example of the ramifications when there is a gap. Both parties should carefully review the policies in place, and carefully compare the coverage language (including any exclusions) with the lease language.

[7] *Sears. Roebuck & Co. v. Charwil Associates, Ltd. Partnership*, 371 Ill. App. at 1078 (2007).

Concerns that Affect both Property and Casualty Coverage.

Most insurance related issues carry the potential to touch both property and casualty coverage, particularly when including general concerns about ensuring that the policy covers the scope of property, time and activities as the lease. Such issues may include (though most certainly are not limited to) the following:

ASSIGNMENT OF LIABILITIES – ASSIGNMENT OF COVERAGE?

Many leases allow one or both parties to assign their rights under the lease. Typically the landlord reserves the right to assign their interests at any time without affecting the lease, while the tenant's rights to assignment are subject in some way to the landlord's approval. Either way, it is imperative that the parties wrap insurance concerns into any assignment. Insurance policies rarely allow for coverage to be assigned.[8] Failure to properly transfer the insurance to the new person or entity, to add the assignee as an additional insured or loss payee, or to procure new insurance, can create a gap in coverage.

The lease should specify that the assignee shoulder all insurance rights and obligations in the lease (as well as most other obligations under the lease), and that the parties take whatever steps are necessary to ensure seamless coverage.

> ***Practice Tip:*** As a follow up to the prior tip on the issue of making sure the coverage promised was actually procured, the wise party on the other side of the table from the assignor will ensure that they get new proof of insurance from the assignee so that they can establish that there is in fact a new policy in place covering the appropriate parties. This is also important when the assignee party is simply another corporate form of the assignor party.

If the lessee is allowed to sublease the premises, the lease should clearly indicate any liability and attending insurance burdens. The belt and suspenders approach for the landlord requires the original lessee to remain ultimately liable for their original obligations, including any obligations to carry insurance. Likewise, the prudent landlord will want to contemplate requiring that any insurance carried by the sub-lessee will name both the lessee/sub-lessor and the primary lessor as additional insureds or loss payees.

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[8] Courts will tend to strictly enforce anti-assignment clauses when the policy rights are assigned before a loss, as such an assignment may increase the insurer's risks. Courts may well, however, uphold an assignment made after a loss, depending in part on the exact language of the policy, as assignment of an existing claim does not pose any additional risk to the insurer. For further discussion on the issue of assignment of insurance policies, *see* 17 Williston on Contracts § 49:126 (4th ed. 2007).

One issue to be wary of: where both the lessee/sub-lessor and the sub-lessee are to carry insurance policies covering losses relating to the property or the leasehold, this creates a potential for the lessee's and sub-lessee's insurance policies to point a finger at the other as the primary policy responsible to cover a particular loss. This can engender lengthy and thus costly coverage battles that may impede the ability to timely recover for any loss. A well drafted lease makes it clear which insurance policy is to be the primary policy in the case of a sub-lease, and requires that the sub-lease contract itself include the requisite language clearly reflecting this requirement. Again, it is wise for all parties to review the certificates of insurance, applicable policies and any endorsements once issued to ensure that the policy coverage issued provides the coverage intended and required.

EXTREME CIRCUMSTANCES, EXTREME DAMAGES.

There have been a flood of cases and articles relating to insurance coverage for extraordinary catastrophic acts, be they natural (Hurricane Katrina) or by act of man (9/11 and Y2K). This is a complex subject far beyond the scope of these materials.[9] Suffice to say that a tightly drafted commercial lease will consider the effects of such an unusual event, because while rare, the effects are devastating for all involved. The standard insurance policy will not cover such unusual risks. In addition, a general lease provision requiring that the tenant (or landlord) procure basic property or casualty coverage, or even extended coverage against fire and other risk, does not typically require that the tenant (or landlord) obtain coverage for such extreme events such as terrorism.[10] Therefore, failure to procure such coverage will not be deemed a default. And, most critically on a practical level, it means that there is no coverage for what is surely a devastating loss.

Geographical areas and location of the premises are key factors in assessing relative risk, though a higher risk typically means that the premiums for coverage will be correspondingly higher. The parties may not find it economically worthwhile to insure against a remote possibility; however, at a minimum, prudent landlord and tenant counsel will clearly allocate who bears what risk in the event of such a disaster. Whether or not to require insurance, and in what form, will vary according to the relative risk both of such an occurrence happening, and the financial impact on the parties if it did. Whether or not such clauses are ultimately included in a lease, the parties must at least consider the issue before making a decision.

SUCCESSOR LIABILITY AND AVAILABLE INSURANCE

Recent cases in several states have addressed the accessibility of coverage for successor companies. The trend suggests there may be possibilities for tapping into insurance

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[9] For a few excellent articles on insurance and extreme loss events, *see* Jo-Ann M. Marzullo, Economic Catastrophes: Real Estate in the Wake of Dot.coms, Recession and Terrorism, ABA 2002 Annual Spring Symposia; Ross Green, Catastrophic Service Interruption in Commercial Leases, ABA Probate & Property January/February 1994 at 6.

[10] *See, e.g., TAG 380, LLC v. ComMet 380 Inc.,* 830 N.Y.S.2d 87 (N.Y.App.Div.1.Dept. 2007).

policies issued to related companies to cover claims for a defendant company that is now defunct, or that has inadequate coverage for a particular loss.[11] While the court battles continue over just how far coverage for one company will extend over ill-defined lines between either successor or related companies, the prudent lawyer may wish to allow as broad of access to insurance coverage as possible by identifying all related companies in the lease, and requiring that all closely related companies of either lessor or lessee be named as additional named insureds in any required policies.

COVERAGE FOR DISCRIMINATION, EMPLOYMENT LAW VIOLATIONS, ADVERTISING, AND OTHER SEEMINGLY UNRELATED PROBLEMS

Landlords must obviously be diligent to ensure that the tenant retains full responsibility for any liabilities that may arise out of their business. Such liabilities may include employment related liabilities, labor related liabilities, and business marketing liabilities. What landlords must not forget is that insurance matters here, too. Landlords must be diligent in ensuring that the tenant retains appropriate coverage, not only for ultimate liability but also for defense of any claims that may be asserted against the landlord. An advertising claim, for example, may be asserted against the landlord if it involves signage on the property, particularly if the sign is part of the real property that is the subject of the leasehold. A creative complainant's counsel in a discrimination suit or personal injury suit arising out of an injury sustained at the workplace may add in the landlord if there is any indication that the landlord knew of an illegal or dangerous condition and failed to take steps to remedy it. The landlord must thus ensure not only that the tenant promise to defend and indemnify the landlord for any such claims, but also that the tenant carries sufficient insurance to aid in both roles.

Similarly, the tenant must be sure that any liabilities that are to be born by the landlord include a requirement not only that such liabilities are insured, but also that the contractual duty to defend is also covered by the landlord's insurance policy.

SELF-INSURANCE.

If there is no requirement for insurance to protect the property, then the risks are de facto self-insured.[12] This means that the party responsible for the damage under the lease must pay for the loss themselves. This may be a viable option for some losses and in some situations, but it also carries an obvious significant risk if the responsible party does not have the resources to timely cover the loss. Aside from simply omitting the insurance requirement altogether or where a party neglects to procure the required insurance, there are myriad of less

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[11] For an excellent article on one such case, *Henkel Corp. v. Hartford Accident & Indemnity Co.*, 62 P.3d 69 (Cal. 2003), see Patrick Hofer's article "Corporate Succession and Insurance Rights after *Henkel*: A Return to Common Sense" recently published in the ABA Tort Trial & Insurance Practice Law Journal, V. 42 No. 3 at page 763 (2007).

[12] For an excellent article on self-insurance, see Ann Peldo Cargile's article in the September/October 2001 issue of ABA's Property & Probate, The Perils of Self-Insurance in Leases.

obvious way for your clients to find themselves in a de facto self-insured situation. This may happen where an insurance policy excludes or limits the loss in question; where the insured party is not the party liable for the loss; where the liability to be covered is an excluded event, and there is no suitable endorsement to close this gap in coverage; where the deductible is substantial; or where the insured is underinsured or runs into coinsurance issues.

It may also happen when policies collide. For example Party A, who is designated the responsible party for a particular loss in the lease, has an insurance policy that is deemed secondary to Party B's insurance policy. This may happen when Party B bears some residual liability under the contract, sufficient to trigger potential for coverage under Party B's own insurance policy and thus negating the ability to reach Party A's policy. Such situations are best avoided through careful review of both the lease language and the allocation language within the applicable insurance policies.

TIME LIMITS IN LEASE VERSUS POLICY SUIT LIMITATIONS

Insurance policies tend to include suit limitations, and courts will typically enforce such provisions, even in government contracts.[13] Both lessor and lessee must wary of the potential of one or the other procuring a policy that includes such limits. The practical effect of such limits may be that an otherwise covered loss may fall within the applicable statute of limitations for whatever type of claim it may be, but fall outside the suit limitations imposed by the insurance policy. This would essentially render the loss as un- or self-insured.

ENVIRONMENTAL LIABILITIES.

The arena of environmental liabilities warrants a thesis of its own, is much too broad to cover here, and much too varied for any meaningful summary remarks. Suffice to say that the parties must carefully consider not only how environmental liabilities are to be allocated, including claims that arise out of the actions of the tenant or out of actions of the landlord preceding the tenant's occupancy, but also how such liabilities are to be insured. Environmental claims are frequently excluded or severely limited in the standard policies without the appropriate endorsements. Therefore, the lease should clearly delineate the desired scope of environmental coverage.

In addition, the parties must carefully consider requirements for insurance coverage for defense for environmental claims. All litigation is expensive. But dealing with environmental claims may top the list of some of the most expensive and arduous types of claims to defend. Therefore, the ideal lease will carefully allocate who will pay for defending such claims, and ensure appropriate insurance coverage that will cover such a defense for all parties. In addition, the parties all have an interest in ensuring that any applicable policy will recognize a duty to defend as early as possible once any claim is made that may lead to liability for environmental

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[13] *See, e.g., Evergreen Park School Dist. No. 124 v. Federal Ins. Co.*, 658 N.E.2d 1235 (Ill.App. 1 Dist.,1995).

problems. In drafting such language, the practitioner would be wise to reference whatever the current state is of voluminous and ever increasing case law regarding when an assertion of liability for environmental matters is sufficient to be considered a covered "claim" or "suit."l[14]

ALLOCATION OF LIABILITY FOR ONE'S OWN NEGLIGENCE.

Aside from protecting the parties from excessive liabilities, insurance can also be an important tool in facilitating the allocation of respective responsibilities between landlord and tenant. Of particular interest is the role of insurance in allowing an allocation of liabilities that may be otherwise legally void as against public policy. For example, public policy (and in some cases specific statues) generally prohibits any party from disclaiming liability for their own actions or negligence.[15] A landlord who disclaims any liability arising from a condition on the property that was caused by the landlord's actions may discover that the court will void such a disclaimer as contrary to public policy. However, where such disclaimer is coupled with an allocation of responsibility to the other tenant, and a requirement that the tenant insure against just such a potential loss, the courts have found that as the loss is still covered that the disclaimer and shifting of liabilities is no longer void as against public policy.

Two 2007 cases illustrate how this may play out even when the public policy aspect is not a specific issue on the table. In the Sears case discussed above (371 Ill. App. 3d 1071), the court did not specifically address the validity of allocation of responsibility for one's own negligence. In dicta it did, however, discuss the fact that the lease requirement essentially held the landlord liable for the tenant's own negligence. In that case, again, the accident occurred in the common area for which the landlord assumed liability, but was an injury caused by the tenant's employee while driving another customer's car. The landlord attempted to argue that the parties never intended to pass off liability for the tenant's own negligence, and had an expert opine that he had never seen such a requirement before. The court disregarded this issue altogether, finding that the lease was unambiguous and thus did not require looking outside the four corners to interpret the intent of a promise to indemnify for "any and all" claims– thus, upholding the allocation of insured liabilities.

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[14] There is vigorous ongoing debate, and resulting variation in the case law, regarding when a claim constitutes a "suit" for purposes of the duty to defend in environmental cleanup cases. The results will vary widely depending on the facts, the policy language, and the local court trends. For a few of many discussions on the topic, *see, e.g..,* Lee R. Russ in consultation with Thomas F. Segalla, 14 Couch on Ins. § 201:13 (3d ed. 2007); *Aetna Cas. & Sur. Co. v. Com.,* 179 S.W.3d 830 (Ky. 2005); Mitchell L. Lathrop, Insurance Coverage for Environmental Claims § 3.04 AT 3-45 (1992).

[15] *See, e.g., Great Northern Ins. Co. v. Interior Const. Corp.*, 796 N.Y.S.2d 51 (N.Y.A.D. 1 Dept. 2005)(lease provisions negotiated between sophisticated parties negotiating at arm's length that allocate risk of liability to third parties through insurance, are enforceable, even where such clauses purporting to exempt party from liability for its own negligence are generally void as against public party); *Duane Reade v. 405 Lexington, L.L.C.*, 800 N.Y.S.2d 664 (N.Y.App.Div.1.Dept. 2005)(requirement for tenant to procure insurance that would shield landlord from liability did not violate General Obligations Law that declares clauses exempting landlords from liability for injury to property void as against public policy).

In contrast is Rouse-Miami, LLC v. Bentley's Luggage Corp. from the Florida Appellate Court.[16] There, the lease obligated the tenant to indemnify the landlord in connection with personal injury "suffered by third parties arising from or out of" the tenant's occupancy. The lease excluded employees from being third-parties. One of the tenant's employees sued the landlord for injuries sustained in the parking lot, claiming inadequate security. The court found that a tenant was not obligated to indemnify the landlord for a tenant employee's claims of landlord negligence, given that the indemnification provision specifically excluded employees. In addition, the court noted that the lease did not clearly state the intention to indemnify the landlord for liability for its own negligent acts. The court held that any attempt to indemnify the indemnitee for its own negligent acts must be expressed in clear and unequivocal terms."[17]

Insurance can be a useful tool to allocate respective liabilities. But to ensure that such a provision will not be deemed unenforceable, prudent parties will ensure that the lease clearly identifies those areas where the parties do in fact intend for one to transfer liability for its own acts to the other, and make sure insurance is required (and in place) to cover the loss.

FINAL PRACTICE TIPS:

Do be sure to **get in the details**. Accidental omissions or failure to fill in details in a standard form can serve to preclude a party's right to the insurance they expected. For example, where insurance requirements are too vague to determine exactly what type or scope of insurance was required, and where the parties have no history of dealings such that the meaning of an ambiguous insurance requirement might be fleshed out, such a provision may be deemed unenforceable altogether.[18]

As with any other type of insurance, it is imperative to ensure that the **policies in place cover all intended losses**, which may require additional endorsements to cover specific or commonly excluded perils. Endorsements are often required to ensure adequate coverage for property and other damages flowing from floods or other natural disasters, vandalism, terrorism or government takings of the property, or other major events. The parties should consider the exact scope of property to be covered by either tenant or landlord – both actual property to be protected against damage (property coverage) and the scope of premises from which liabilities may arise (casualty

[16] 948 So.2d 928 (Fla.App.3.Dist., 2007).

[17] *Id.* at 929.

[18] *See, e.g, Gallogly v. Kurrus*, 905 A.2d 1245 (Conn. App. 2006)(requirement that tenant provide "public liability insurance" was so vague and indefinite as to be unenforceable, and thus tenant did not breach lease for failure to procure such insurance); *see also McEewan v. Mountain Land Support Corp.*, 526 Utah Adv. Rep. 28 (Utah App. 2005)(where commercial lease had subtitle "Property Insurance," the substantive language in that section referenced only casualty insurance; therefore, the lease was unambiguous as to the *lack* of any obligation of the tenant to procure property insurance).

coverage). Some examples of situations where the parties must take particular care are where the landlord's total property exceeds the space actually being used by the tenant; where the tenant has made some substantial improvements to the premises; or where the landlord and tenant are engaged in any joint operations.

In addition to ensuring that there is sufficient coverage, it is also prudent to **ensure there is not duplicative coverage**. Having both parties carry coverage for the same loss is an unnecessary waste, particularly when the policies cannot be stacked. In addition, it may create unwanted problems down the road when the respective carriers each claim the other bears primary responsibility. This latter concern can be remedied with careful consideration of the multiple policy priority provisions in each policy, but so long as the coverage carried by one party or the other is sufficiently broad in scope (both regarding scope of claims covered and total amount of coverage dollars available) to satisfy the lease, duplicative policies only benefit the insurance companies cashing in the premium checks.[19]

The questions of "who is liable for what" – and who carries the insurance to cover it – get particularly complicated in any case involving common areas for which both landlord and tenant share responsibilities (and thus liabilities).[20] Therefore, the parties and their legal counsel must carefully review the lease to ensure that there is complete coverage, but without being unnecessarily duplicative. Where there may be some overlapping in coverage for security in less well defined arenas such as common areas, as certainly some overlap is preferential to gaps, the parties should specifically identify which party's insurance policy is to be determined "primary," and require that the policy recognizes this as well.

The courts will typically find that **failure to procure the required insurance constitutes a material breach of the lease**,[21] though whether the breach warrants forfeiture or other such extreme measures will depend on the exact provisions of the

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[19] For additional discussion on the identification of proper insureds, and the wisdom of avoiding duplicative insurance, *see* Cargile, Digging Into Ground Leases: Insurance and Reconstruction Issues, ABA Property & Probate March/April 2006 at 42, 44.

[20] *See, e.g., Sears. Roebuck & Co. v. Charwil Associates, Ltd. Partnership*, 371 Ill. App. 3d 1071 (1 Dist. 2007)(where lease required landlord to procure insurance for all liability arising from use of common areas, and where lease obligated landlord to defend and indemnify the tenant against "any and all claims" related to a tenant's customer's use of the common areas, the landlord breached its promise to provide insurance even though it did not breach its promise to indemnify, where CGL policy did not cover a claim that arose from one of the tenant's customer's use of the common area).

[21] *See, e.g., Jackson 37 Co., LLC v. Laumat, LLC,* 830 N.Y.S.2d 281 (N.Y.App.Div.2.Dept., 2006); *see also* John Francis Major, J.D., Material Breach of Commercial Lease, 7 AM JUR POF 3d 655 § 16 (2007).

lease.[22] A default may even occur where a party procures a policy with a substantial deductible, if such a deductible violates the overall insurance requirements.[23] This is particularly true where the lease specifically identifies failure to procure the required insurance as an event of default. Unlike other forms of potential default, the courts have also affirmed that there is no obligation to cure such a failure.[24] Once the failure has occurred, there is no way to go back in time and remedy the gap in coverage. Thus, the parties are well advised to be sure to procure all required coverages. Otherwise, they may find themselves responsible for a default and termination of the lease, and in turn liable for damages that go well beyond the loss that was supposed to be insured.

Finally, the parties must ensure that the **covered losses match up with the assumed responsibilities**. For example, if the landlord is responsible for repairing any major damage to an HVAC system, the landlord must be the one required to carry the requisite property coverage. If the tenant is to assume all liabilities and duty to defend both tenant and landlord for any personal injuries claimed arising out of physical injury occurring on the premises during the tenancy, the tenant must be the one required to carry the requisite casualty coverage.

These issues may seem rudimentary, but too often through the various evolutions of a lease draft the parties' obligations may shift in one section, without an appropriate revision of the insurance requirements for coverage of those obligations. Cross-referencing the damages each party is responsible for to the insurance to be carried by each party is a critical component of any final lease review.

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[22] *See, e.g., Metropolitan Transportation Authority v. Kura River Management, Ltd.*, 739 N.Y.S.2d 668 (N.Y.A.D. 1 Dept. 2002)(tenant's failure to acquire and maintain required insurance did not warrant forfeiture, where notice of default had not given adequate notice of such a claim and default had been cured).

[23] *See, e.g., Rouse-Miami, LLC,* 948 So.2d at 930 (Fla. App. 2007)

[24] *See, e.g., Jackson 37 Co., LLC,* 830 N.Y.S.2d (2006).

Angelia D. Wesch is a member of Eisenhower & Carlson PLLC, a Pacific Northwest law firm with offices in Tacoma and Seattle, WA. Ms. Wesch counsels real estate developers, condominium associations and construction clients on land use, transactional and litigation matters. Ms. Wesch has extensive experience resolving multi-million dollar construction defect disputes and providing insurance coverage advice for corporate and individual policyholders. A frequent speaker on real estate and insurance coverage issues, Ms. Wesch currently chairs the firm's Executive Committee and its Real Estate and Land Use Practice Group. Ms. Wesch is Past-President of CREW Seattle and previously served on the Board of Directors of CREW Network. Ms. Wesch also serves on the Economic Development Board for Tacoma/Pierce County.

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