

**INSURANCE AND INDEMNITY IN REAL ESTATE TRANSACTIONS
(DRAFTING INSURANCE REQUIREMENTS
FOR LEASES/DEVELOPMENTS/WHATEVER)**

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CHAPTER 10

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INSURANCE AND INDEMNITY IN REAL ESTATE TRANSACTIONS: (DRAFTING INSURANCE REQUIREMENTS FOR LEASES/DEVELOPMENTS/WHATEV ER)

§ 10.01. DEFINITIONS

A. Indemnity

An indemnity is an undertaking by one party to a contract (1) to protect the other party against the occurrence of hurt, loss, or damage and (2) to compensate the other party if the hurt, loss, or damage actually occurs. Insurance professionals refer to indemnities as *hold harmless agreements*, a phrase derived from the usual wording of an indemnity:

"hold harmless and defend [indemnitee] against."

An indemnity is an *affirmative* obligation in the sense that an indemnity creates a cause of action against the indemnitor.

B. Waiver

A waiver is an agreement by one party to a contract not to hold the other party responsible as to certain types of liability arising out of the transaction. A waiver is *negative* in nature in the sense that it operates to bar any cause of action on the released matter.

C. Insurance Defined

An insurance policy is a contract under which a company in the business of insuring against losses undertakes to compensate the party for losses (and sometimes defend a party against claims) arising from specified risks for a stated period of time in consideration for the payment by the insured party of a premium. To risk managers, insurance is a financial transfer of risk, *i.e.*, the payment of a relatively small amount to transfer the risk of a potentially large, uncertain risk.

§ 10.02. INDEMNITY/WAIVER PROVISIONS

A. Types of Indemnities

Insurance professionals generally describe indemnities as being "limited", "intermediate," or "broad."

1. Limited

A "*limited*" indemnity clause imposes liability upon the indemnitor only to the extent of the indemnitor's fault or negligence and is the most favorable type of indemnity clause for an indemnitor.

2. Intermediate

Under an "*intermediate*" indemnity clause, the indemnitor assumes all liability except for the sole negligence of the indemnitee.

3. Broad

A "*broad*" form indemnity clause imposes the entire risk of loss upon the indemnitor, including the sole negligence of the indemnitee, and is the most favorable type of indemnity clause for an indemnitee.

4. Split

Statutes such as Chapter 151 of the Texas Insurance Code have produced a new category of indemnity. Section 151.102 provides that a provision in a construction-related contract

"is void and unenforceable as against public policy to the extent that it requires an indemnitor to indemnify, hold harmless, or defend a party, including a third party, against a claim caused by the negligence or fault ... of the indemnitee, its agent or employee, or any third party under the control or supervision of the indemnitee."

Hence, the statute appears to permit only limited indemnities in construction-related parties. However, Section 151.103 expressly excludes "claims for the bodily injury or death of an employee of the indemnitor, its agent, or its subcontractor of any tier." Thus, broad form indemnities are permitted with respect to third party over actions. This dichotomy has led to the drafting of indemnities which are partially broad form and partially limited form.

B. Reasons for Using Indemnities or Waivers

Both indemnities and waivers shift financial responsibility for losses from the parties that normally would or might be financially responsible for the losses to other parties. Among the reasons for using an indemnity or a waiver are the following:

- a) The other party may be in a better position to finance the risk or control the exposure;
- b) One party wants to protect and hold down the overall cost of its insurance program or is not insured (*i.e.*, wants the other party's insurance program to answer or, at a minimum, to answer first);
- c) The risk is customarily allocated to one of the parties within an industry; or
- d) The bargaining position of one party is strong enough to enable it to shift the responsibility for the loss to the other party.

C. Drafting Considerations

The drafting of indemnities and waivers requires care. At a minimum, the following questions should be considered when drafting an indemnity or waiver:

- a) Does the party giving the indemnity or waiver have proper authority or capacity to enter into the indemnity or waiver?
- b) What is the creditworthiness of the indemnitor? Is a guaranty, bond or insurance necessary?
- c) Should persons other than the contracting parties (*e.g.*, shareholders, directors, officers, agents, and employees) benefit from the indemnity or waiver?
- d) Will liabilities arising out of the actions or omissions of persons other than the party giving the indemnity or waiver (*e.g.*, agents, employees, contractors, subcontractors, subtenants, or invitees) be subject to the indemnity or waiver?
- e) Is the recovery against the party giving an indemnity limited as to amount, ability to seek a deficiency judgment, or source of funds to pay damages?
- f) What risks are covered by the indemnity or waiver?
- g) Is the indemnity or waiver consistent with insurance coverages carried by the parties both as to amounts and risks insured?
- h) Is the obligation to defend and the entire cost of defense included in the indemnity or waiver? If so, will the beneficiary of the indemnity or waiver be entitled to separate counsel of the beneficiary's choosing?
- i) Are there any types of damages (*e.g.*, punitive, special, exemplary, or consequential) excluded?
- j) Are there any limitations as to the time period the indemnity or waiver will be in effect or the time period for making a claim under the indemnity or waiver?
- k) If the transaction is governed by Texas law, is compliance with the so-called Fair Notice

Doctrine necessary (or in many other states, is compliance with the "Clear and Unequivocal Doctrine" necessary)?

- l) Do any anti-indemnity statutes apply?

D. Potential Pitfalls

1. Anti-Indemnity Statutes and Law

At least 40 states plus the District of Columbia currently have some form of anti-indemnification statutes, most of which are construction-related. For example, Chapter 151 of the Texas Insurance Code imposes major limitations on broad form indemnities in contracts relating to the design, construction, alteration, renovation, remodeling or repair of structures.

2. Insurance Limitations

Unless an indemnity covers an insurable risk under the indemnitor's insurance and the contract has been written in a way that the indemnitee can avail itself of the indemnitor's insurance, an agreement to indemnify does not involve insurance and is solely a contractual agreement between the indemnitor and indemnitee. Insurance companies may be unwilling to provide coverage for some indemnified losses (*e.g.*, the sole negligence or strict liability of another party). Even when indemnities are covered by insurance, liability under indemnities is typically unlimited as to amount (all insurance policies have limits) and the scope of contractual indemnities is commonly broader in scope (*e.g.*, "any and all" losses) than any possible insurance program. The insurance industry has always imposed some limitations on coverage under an insurance policy for liability assumed by the named insured under a separate contract (*i.e.*, so-called contractual liability). Even when exceptions are made to the exclusion for liability assumed under separate contract, the assumed liability which is not excluded is restricted to bodily injury and physical injury to tangible property and is subject to policy exclusions and limitations contained elsewhere in the policy. Contractual liability is discussed in § 10.05[B][4].

a. *Defense of Indemnitee May Not Be Covered or May Erode Policy Limits*

Indemnity provisions in contracts generally include an obligation to defend, but the cost of the defense may not be covered by the indemnitor's insurance. Under the current edition of the ISO form of commercial general liability insurance, the insurance company is only required "to defend *the insured* against any 'suit' seeking damages." In order for the indemnitee's defense to be covered the indemnity must be contained in "a contract or an agreement that is an 'insured contract,'" as the term is defined in the policy, and the cost of the defense must have been assumed within the indemnity. See discussion at § 10.05[B][4].

The ISO form of commercial general liability policy states that "Solely for the purposes of liability assumed in an 'insured contract,' reasonable attorney fees and necessary litigation expenses incurred by or for a party other than an insured are *deemed to be damages because of 'bodily injury' or 'property damage.'*" For example, if the policy has a \$1 million each occurrence limit for damages arising out of a single accident and \$500,000 is expended to pay indemnitee's "reasonable attorney fees and necessary litigation expenses," only \$500,000 will remain to pay damages to the injured party. ISO commercial general liability insurance form, CG 00 01 includes a lengthy list of additional conditions, which, if met, cause the attorneys' fees and costs of the indemnitee to be paid outside the policy limit, *i.e.*, the reasonable attorney fees and necessary litigation expenses incurred by or for the indemnitee will not be deducted from the limits under the policy. If the conditions are met, in the example given above, the entire \$1 million each occurrence limit would be available to pay damages to the third party. However, meeting all of the conditions is difficult.

b. Bars to Recovery

Under certain circumstances, the liability of a party to a contract could be limited by statute or under case law. One such limitation is created by the exclusive recovery rule under workers compensation acts. In addition some comparative negligence statutes bar recovery from joint tortfeasors.

E. Fair Notice Doctrine (Texas)

In Texas most broad form indemnities and waivers (*i.e.*, indemnities against, or waivers of, liability arising out of one's own negligence) are permitted but are subject to the "Texas Fair Notice Doctrine," a judicially developed standard consisting of two distinct rules: the "express negligence rule" and the "conspicuousness rule."

1. Express Negligence Rule

If the parties to a contract desire to indemnify one of the parties against its own negligence, the parties must express the intent in specific terms within the four corners of the contract. *Ethyl Corp. v. Daniel Constr. Co.*, 725 S.W.2d 705, 707 (Tex. 1987). The express negligence requirement is a rule of contract interpretation and therefore determinable as a matter of law. *Fisk Elec. Co. v. Constructors & Assoc., Inc.*, 888 S.W.2d 813, 814 (Tex. 1994). A benefit of changing forms to comply with the Texas express negligence rule is that expressly stating the intent should comply with the clear and unequivocal requirement in most other states (assuming, of course, that the indemnity or waiver is not specifically barred by an anti-indemnity statute).

2. Conspicuousness Rule

A provision containing the indemnity against one's own negligence must be conspicuous, *e.g.*, a clear or informative heading, LANGUAGE IN CAPITAL LETTERS, **language in contrasting type or color**, and indemnity provisions separate from provisions dealing with other topics. *Fisk Elec. Co. v. Constructors & Assoc., Inc.*, 888 S.W.2d 813, 814 (Tex. 1994).

§ 10.03. INSURANCE POLICY FORMS

A. ISO Forms

Insurance Services Office, Inc., commonly known in the insurance industry as *ISO*, drafts insurance policy forms that are used either verbatim or with some modification in all 50 states. In the property and liability insurance industry ISO forms serve as the standards against which non-ISO forms are compared, much in the same way as AIA (American Institute of Architects) forms serve as the benchmarks in the construction industry. Although ISO policy forms are still dominant in most fields, other policy forms exist which are:

- 1) "manuscripted," *i.e.*, drafted by the insurance company,
- 2) dictated by a government agency, *e.g.*, policy forms under the National Flood Insurance Program, or
- 3) drafted by an ISO competitor, *e.g.*, American Association of Insurance Services.

Many real estate documents incorrectly reference the National Board of Fire Underwriters, an entity created by fire insurance companies in 1866 to reduce the risk of fire in buildings. In 1965 the Editions

Numerous editions of insurance policy forms have been published by ISO, each edition providing a different level of coverage. Edition identifiers are found in the lower left corner of each insurance form and generally contain a pair of capital letters followed by four pairs of numbers, *e.g.*, CG 00 01 04 13. The ten-digit numbering sequence of ISO forms and endorsements has a very specific meaning:

- The first two entries are letters that indicate the line of insurance involved. For example, CG denotes commercial general liability insurance and CP denotes commercial property insurance.
- The next two digits in the sequence designate the specific insurance category. The categories for commercial general and commercial property insurance are set forth in **Appendix G**. Endorsements are grouped in categories according to their purposes.

- The next two digits in the sequence are the form or endorsement number within the insurance category.
- The last four digits in the sequence are the edition date of the form or endorsement expressed in month and year format.

If the policy form is an unmodified ISO form, the phrase "Copyright Insurance Services Office [date]" or "© Insurance Services Office [date]" should appear at the bottom of the page. If modifications have been made, a reference should appear to the effect that the form contains provisions from the copyrighted ISO form.

For reasons to be discussed below, the author recommends the use of ISO form identifiers in the insurance provisions of real estate documents, but a drafting problem may arise because edition dates change, often more than once during the term of a lease or mortgage. The insurance industry tends to use the most recent edition of a particular policy form and clients are generally more interested in establishing a benchmark for the type of policy rather than a specific edition of the policy. Hence, the author generally omits the edition date from the ISO form identifier and instead use a phrase such as "the most recent edition of ISO form CG 00 01, or its equivalent" and a catch-all provision to the effect that if the forms of policies, endorsements, certificates or evidence of insurance required by the contract are superseded or discontinued, the client will have the right to require other equivalent forms.

B. Insurance Coverages in General

Three general categories of commercial insurance are relevant to real estate attorneys: property insurance, liability insurance and package coverage insurance.

1. Property Insurance

Property insurance is "*first party*" insurance that compensates the insured for property belonging to the insured that has been lost, damaged, or destroyed. To real estate attorneys, the "property" in question will usually be buildings, leasehold improvements, fixtures and equipment located in buildings, and the income derived therefrom.

a. *Categories*

The insurance industry has largely abandoned use of the words *risks* and *perils* and instead uses the term *causes of loss*. Historically, property insurance was written either on (1) a *named peril* basis which insured property against loss or damage from causes of loss expressly enumerated in the policy, or (2) an *all risks* basis which insured property against loss or damage from all causes of loss except those that were expressly excluded by the policy. The proper terminology for this

general category of insurance is *property insurance*, not *fire and extended insurance* or *casualty insurance*. *Fire and extended coverage insurance* was a named peril property insurance which is no longer available. *Casualty insurance* in the insurance industry means all types of insurance *except* life insurance and *property insurance*.

b. *Examples*

Examples of property insurance policies are commercial property, builders risk, flood, earthquake, equipment breakdown (formerly known as "boiler and machinery"), business income and extra expense, and business income/rental value insurance properties.

2. Liability Insurance

Liability insurance is *third party* insurance that compensates a party injured by the actions or omissions of an insured. Examples of liability insurance are commercial general, business auto, workers compensation, employers liability, environmental, umbrella, excess liability, and professional liability (errors and omissions) insurance policies.

3. Package Coverage Insurance

Package coverage policies cover both property risks and liability risks. An example of a package coverage insurance policy is the business owners insurance policy.

§ 10.04. PROPERTY INSURANCE

A. **Commercial Property**

As a general rule commercial property insurance is used to cover completed buildings and builders risk insurance is used to cover buildings under construction, or, in some cases, under extensive renovation.

No bright line exists as to when builders risk insurance should be used rather than commercial property insurance. As will become apparent from the discussion in § 10.06[A], builders risk policies have several important advantages over commercial property policies with respect to coverage for buildings under construction.

1. Covered Property

ISO commercial property policies define "Covered Property" as (1) "buildings" and (2) "business personal property."

a. *Building*

A "*building*" is defined as a "building or structure" and *includes*:

- 1) Completed additions;
- 2) Fixtures;
- 3) Permanently installed machinery and equipment;
- 4) Personal property owned by the named insured and used to maintain or service the building (*e.g.*, fire extinguishers and floor coverings); and
- 5) If not covered by other insurance, additions under construction, alterations and repairs to the building, and materials, equipment, supplies, and temporary structures, on or within 100 feet of the described premises, used for making additions, alterations or repairs to the building or structure.

Some of the types of property that real estate practitioners would consider to be real property but which are *excluded* from ISO's definition of the term Covered Property include the following:

- a) Land (including the land on which the property is located), water, growing crops or lawns;
- b) Foundations of buildings, structures, machinery, or boilers, if the foundations are below the lowest basement floor, or the surface of the ground, if there is no basement;
- c) Bridges, roadways, walks, patios, or other paved surfaces;
- d) Bulkheads, pilings, piers, wharves, or docks;
- e) Underground pipes, flues, or drains;
- f) Retaining walls not part of the building; and
- g) Cost of excavations, grading, backfilling, or filling.

b. Business Personal Property

"Business personal property" refers to the personal property located within a building and out in the open within 100 feet of a building and *includes*:

- 1) Personal property of others;
- 2) The named insured's use interest as tenant in improvements, and betterments, (*i.e.*, fixtures, alterations, installations);
- 3) Machinery and equipment;
- 4) Stock, *i.e.*, merchandise held in storage or for sale, raw materials and in-process or finished goods;
- 5) All other personal property owned by the named insured and used in its business;
- 6) Labor, materials, or services furnished by the named insured on the personal property of others;
- 7) The named insured's use interest as tenant in improvements and betterments (*i.e.*, fixtures, alterations, installations, or additions to a

structure occupied but not owned by the named insured which are acquired or made at the expense of the named insured but are not legally removable by the named insured); and

- 8) Leased personal property for which the named insured has a contractual responsibility to insure.

The proper terminology is "Business Personal Property" not "contents."

Excluded from the definition of Business Personal Property are several items considered to be personal property in a non-insurance context:

- a) Accounts, bills, currency, money, notes, securities, or other evidence of debt;
- b) Animals;
- c) Automobiles held for sale;
- d) Contraband;
- e) Personal property while airborne or waterborne;
- f) Electronic data (*i.e.*, information, facts or computer programs stored as or on, created or used on, or transmitted to or from computer software, floppy disks, CDs, tapes, drives, cells, or data processing devices); or
- g) Vehicles or self-propelled machines that are licensed for use on public roads and are operated principally away from the described premises.

Please note that coverage is available for some of the excluded categories of personal property by endorsement (often requiring payment of an extra premium) or separate policy.

2. Standard Forms of Commercial Property Policies

a. Basic and Broad (Named Peril) Forms

Two named peril commercial property insurance policies are currently available: "*causes of loss - basic form*" (ISO Form CP 10 10) and "*causes of loss - broad form*" (ISO Form CP 10 20). "*Causes of loss - basic form*" covers 12 causes of loss:

- fire;
- lightning;
- explosion;
- windstorm or hail;
- smoke;
- aircraft;
- vehicle collision;
- riot or civil commotion;
- vandalism;
- sprinkler leakage;
- sinkhole collapse; and
- volcanic action.

"Causes of loss - broad form" covers all of the causes of loss covered by the basic form plus the following:

- breakage of glass;
- falling objects;
- weight of snow, ice, or sleet;
- water damage from leaking appliances; and
- collapse from specified causes.

b. *Special (All Risks) Form*

The correct terminology for commercial property insurance written on an all risks basis is "causes of loss - special form" (ISO Form CP 10 30). However, all risks forms do not (and never did) cover *all* risks. Specific exclusions and limitations do apply and should be carefully reviewed. For instance, flood and earthquake are not covered by the causes of loss – special form (unless endorsed).

c. *Burden of Proof*

Under causes of loss - basic form and causes of loss - broad form commercial property insurance, the burden of proof is on the insured to prove that the loss resulted from a scheduled cause of loss. Under causes of loss-special form commercial property insurance, the insured just shows the loss was fortuitous and the insurer has the burden of proof to show that the cause of loss was excluded.

3. Valuation of Covered Property and Amount of Recovery

a. *Co-Insurance*

When a co-insurance percentage applies, a commercial property policy will not pay the full amount of a loss if the replacement cost of the covered property at the time of the loss times the co-insurance percentage is greater than the policy limit. The most commonplace co-insurance requirement is 80 percent. The replacement cost of the property at the time of the loss times the co-insurance percentage equals the minimum amount of insurance required. If the amount of insurance carried is equal to or greater than the minimum required, the insured may recover 100 percent of the loss (less deductible) up to the policy limit. Failure to carry an adequate amount of coverage to comply with this requirement will result in a lower recovery. If the amount of commercial property insurance carried is less than the minimum required, the formula for determining the amount of recovery is :

$$\frac{\text{(policy limit the insured actually carried)} \div \text{policy limit the insured should have carried}}{\text{x amount of loss}} = \text{amount of recovery before application of deductible.}$$

b. *Blanket Insurance*

This form of property policy allows for a single limit of insurance to apply to two or more types of property (e.g., buildings and business personal property) at a single location or multiple locations or a single type of property at multiple locations. Blanket property insurance policies generally have a 90 percent co-insurance requirement.

Traditionally, under a blanket property policy, the total amount of coverage purchased has been available to pay any single loss, so long as co-insurance requirements were met. Hence, the advantage of blanket property insurance is simply stated as "100 percent coverage for 90 percent of the premium." The insured completes a statement of values for the items to be covered, totals up those values, and then insures them all with a single limit of insurance based on 90 percent of the total values (thus complying with the 90 percent co-insurance requirement). If one item is a total loss, the insured recovers 100 percent of the value at the time of the loss, even if that amount of the loss is more than the amount for such location shown on the statement of values. For example, if a real estate portfolio with a total value of \$100 Million had a blanket policy with a limit of \$90 Million, a single building having a normal replacement cost of \$10 Million were destroyed in a far-reaching catastrophe, and the replacement cost of all properties in the affected area sky rocketed by 60% because of the widespread unavailability of labor and materials, the entire \$90 Million would be available to restore the affected building.

Increasingly, however, insurers are adding to blanket property policies so-called "*margin clauses*" (e.g., ISO endorsement form CP 12 32) that limit the maximum amount of coverage available for a single property covered by the blanket policy to a stated percentage of replacement cost for a single building, as shown on a schedule of covered properties.

c. *Actual Cash Value*

The *actual cash value* of a property is the replacement cost of the property at the time of loss with like kind and quality less physical (not book) depreciation. Depreciation may be determined by consideration of age, condition at time of loss, obsolescence and other factors causing deterioration.

d. *Optional Coverage, Replacement Cost*

Replacement cost is the cost of repairing or replacing insured property with comparable materials used for the same purpose on the same site, without reduction for loss of value through depreciation (or as risk managers put it, "new for old"). Replacement cost is determined as of the date of the occurrence. Please note that recovery is the least of:

- 1) the policy limit,

- 2) the cost to replace the lost or damaged property with other property of comparable material and quality and used for the same purpose, or
- 3) the amount actually spent to repair or replace the damaged or lost property.

Until the property is actually replaced, the insured can collect no more than actual cash value.

e. Optional Coverage, Agreed Value

When "agreed value" optional coverage is purchased, the named insured and the insurance company agree upon the replacement cost or actual cash value (as applicable) of the covered property before the policy is written and that co-insurance will not apply. An agreed value endorsement can be used either with an actual cash value or replacement cost commercial property insurance policy and needs annual agreement on replacement cost or actual cash value (as applicable).

f. Debris Removal

The limit of commercial property insurance purchased includes debris removal costs resulting from a covered loss. The debris removal is provided as "additional coverage" and is limited to 25 percent of the sum of the paid loss plus the deductible. An additional limit of \$10,000 is made available by the current edition of the ISO commercial property policy for debris removal if (1) the amount payable under the policy to reconstruct or repair plus the amount payable under the policy for debris removal exceeds the entire policy limit, or (2) the cost of debris removal exceeds 25 percent of the sum of the paid loss plus deductible. Higher limits for debris removal can be purchased by using the Debris Removal Additional Limit of Insurance endorsement (ISO form CP 04 15).

g. Ordinance or Law Coverage

Replacement cost is the cost of replacing the existing structure without consideration to changes in laws or codes. The current edition of the ISO commercial property policy will pay up to the lesser of \$10,000 or 5 percent of the limit of insurance for the increased cost of construction incurred to comply with an ordinance or law in the course of repair, rebuilding or replacement of damaged parts of the covered property. Higher limits can be obtained through the "ordinance or law coverage" endorsement (ISO form CP 04 05). ISO 04 05 also covers the following losses as a consequence of enforcement of an ordinance or law that requires demolition of undamaged parts of the building:

- 1) the loss in value of the undamaged portion of the building and
- 2) the cost to demolish and clear the site of undamaged parts of the building.

B. Special Property Coverages with Respect to Additional Causes of Loss

1. Equipment Breakdown (Boiler and Machinery)

This coverage is available as an endorsement or as a separate policy (e.g., ISO Form BM 00 20 Equipment Breakdown Protection Coverage Form). Equipment breakdown coverage (until 2001 known as "boiler and machinery") is needed because coverage is commonly excluded under commercial property policies for explosion of pressure or vacuum equipment and mechanical, or electrical breakdown of covered machinery and the resulting loss of business income. "Covered Equipment" includes:

- a) Equipment built to operate under internal pressure or vacuum;
- b) Electrical or mechanical equipment that is used in the generation, transmission or utilization of energy;
- c) Communication equipment, and "Computer Equipment" (as defined in the policy).

2. Earth Movement

Coverage is commonly excluded under commercial property policies for loss due to earth movement, including earthquake, landslide, mine subsidence, earth sinking (other than sinkhole collapse), and rising or shifting soil conditions and volcanic eruption, eruptions, explosion or effusion. Coverage can be obtained for earthquake and volcanic eruption through separate earthquake insurance on manuscripted policy forms, a difference-in-conditions, or "DIC," policy¹, or as an endorsement to a property policy (ISO form CP 10 40 with full limit or CP 10 45 with sublimit).

3. Flood

The following exclusion is contained in all three of the ISO causes of loss forms:

g. Water

- (1) Flood, surface water, waves, tides, tidal waves, overflow of any body of water, or their spray, all whether driven by wind or not;
- (2) Mudslide or mudflow;

¹ A DIC policy is an all risks property policy issued by a different insurance company from the company that issued the commercial property insurance policy. The DIC policy

excludes all causes of loss covered by the commercial property policy and covers only the difference between the policies. DIC policies are issued by insurance underwriters experienced in high risk exposures.

- (3) *Water that backs up or overflows from a sewer, drain or sump; or*
- (4) *Water under the ground surface pressing on, or flowing or seeping through:*
 - (a) *Foundations, walls, floors or paved surfaces;*
 - (b) *Basements, whether paved or not; or*
 - (c) *Doors, windows or other openings.*

Hence, without a separate policy or endorsement, the standard commercial property insurance will not cover a flood.

a. Flood Endorsement.

ISO form endorsement CP 10 65 06 07 "Flood Coverage Endorsement" provides coverage for flooding, but usually contains a very high deductible with respect to properties located in a "Special Flood Hazard Area" or "SFHA". SFHA is defined in the National Flood Insurance Program ("NFIP") flood insurance policy discussed below as:

"An area having special flood, or mudflow, and/or flood-related erosion hazards, and shown on a Flood Hazard Boundary Map or Flood Insurance Rate Map as Zone A, AO, A1-A30, AE, A99, AH, AR, AR/A, AR/AE, AR/AH, AR/AO, AR/A1-A30, V1-V30, VE, or V."

However, over 30% of all flood damage occurs outside of Special Flood Hazard Areas. Flood coverage can also be purchased under a DIC policy.

b. NFIP Insurance.

Most flood insurance is written on separate policies issued under the NFIP. The NFIP was established by the National Flood Insurance Act of 1968 [42 U.S.C.A. § 4001 et seq.]. The Flood Disaster Protection Act of 1973 mandated that federally regulated lending institutions could not:

"make, increase, extend, or renew any loan secured by improved real estate or a mobile home located or to be located in an area that has been identified as an area having special flood hazards and in which flood insurance has been made available under the National Flood Insurance Act of 1968"

without flood insurance in an amount equal to the lesser of the loan amount or the available coverage. 42 U.S.C.A. § 4012a(b)(1) (West 2003). Flood Insurance Rate Maps produced by the Federal Emergency Management Agency are used to determine rates.

NFIP insurance has several drawbacks. First, the maximum coverage limits are \$500,000 for a building and \$500,000 for contents.² Hence, the insured that carries flood coverage under its commercial property insurance must coordinate the deductible under the commercial property insurance policy with the limits of the NFIP policy. Second, the policy pays only direct physical loss by or from flood. Thus, indirect or consequential damages, such as loss of income are not covered. Finally, NFIP insurance pays only "Actual Cash Value." However, lenders generally require that commercial property policies contain an optional coverage called "replacement cost", *i.e.*, the cost of repairing or replacing insured property with comparable materials used for the same purpose on the same site, without reduction for loss of value through depreciation.

C. Special Coverages with Respect to Green Buildings

Increased Cost for Green Upgrades (ISO 04 02) was created to deal with the extra costs incurred by an owner when a destroyed or damaged building must be rebuilt as a green building or a damaged or destroyed green building must be rebuilt to a higher standard.

1. Definitions.

ISO's definition of "green" is:

"enhanced energy efficiency or use of environmentally-preferable, sustainable materials, products or methods in design, construction, manufacture or operation, as recognized by a Green Standards-setter."

A "Green Standards-setter" is defined as an organization or governmental agency which produces and maintains guidelines related to Green products and practices. Green Standards-setters include (i) The Leadership in Energy and Environmental Design (LEED®) program of the U.S. Green Building Council, (ii) ENERGY STAR, a joint program of the U.S. Environmental Protection Agency and the U.S. Department of Energy; and (iii) Green Globes™, a program of the Green Building Initiative.

2. Coverages

ISO 04 02 has 3 distinct coverages:

² Austin, William K., "Hurricanes, Tropical Depressions, and Floods – Oh My!", October, 2008, Expert Commentary at www.IRMI.com.

- a) Replacement cost optional coverage in the applicable commercial property insurance policy is expanded to include "Green Upgrades."
- b) Related expenses including:
 - 1) waste reduction and recycling, the expense to reuse or salvage materials and to separate and transport recyclable construction waste,
 - 2) professional fees to LEED-certified architects or engineers for design and consulting during repair or replacement,
 - 3) fees of a Green Standards-setter for certification and expenses to test building systems and equipment during process, and
 - 4) expenses to flush out and/or conduct air quality testing of the renovated space per recommended procedures of a Green Standards-setter.
- c) An extension of the "period of restoration" under business income insurance to include the increased period of time attributable to the Green Upgrade and actions covered by related expenses coverage.

D. Special Coverages with Respect to Indirect Damages

1. Business Income and Extra Expense

This form of insurance (ISO form CP 00 30) provides coverage for loss of earnings (this portion of the coverage was formerly known as "*business interruption insurance*") and/or extraordinary additional expenses incurred, due to a necessary suspension of operations during a period of restoration caused by direct physical loss of or damage to property at the premises described in the policy. Recovery is frequently limited to the length of time required to rebuild or repair the damaged property, plus an additional 30 days to recover business that may have been lost to competitors. The time for this extended period of indemnity can be increased. Business income insurance may be purchased without the extra expense coverage (ISO Form CP 00 32) and extra expense coverage can be purchased without business income insurance (ISO Form CP 00 50).

2. Business Income Rental Value

This coverage is included under both forms of business income forms (ISO forms CP 00 30 and CP 00 32) if the attached declaration so provides. "*Business income/rental value*" protects the landlord against loss of rents during reconstruction and abatement of rentals if the abatement results from a loss under a named cause of loss.

3. Off-Premises Services – Time Element

ISO Form CP 15 45 endorsement to a business income coverage form (with or without extra expense coverage) is needed to provide coverage for the loss of income arising from off-premises utility service disruption, because all of the causes of loss forms (ISO Forms CP 10 10, 10 20 and 10 30) expressly exclude coverage for business income loss caused by "the failure of power or other utility services ... if the failure occurs outside of a covered building"

4. Business Income from Dependent Properties – Broad Form

ISO Form CP 15 08 endorsement to a business income coverage form (with or without extra expense coverage) provides coverage for loss of income (and extra expenses incurred, if applicable) because of damage to another company's facility.

§ 10.05. LIABILITY INSURANCE

Liability insurance is "third party" insurance that compensates a party injured by the actions or omissions of an insured. The core of a commercial liability insurance policy is contained in Commercial General Liability Coverage Form, ISO form CG 00 01 (occurrence basis) or CG 00 02 (claims-made basis). Types of Liability Policies Based on Timing

A. Types of Liability Policies Based on Timing

1. Occurrence Basis

Occurrence basis liability policies cover injuries or damages caused by an "occurrence" that takes place within the "coverage territory", but only if the injuries or damages occur during the policy period, regardless of when the claims are actually made. ISO defines an "*occurrence*" as "an accident, including continuous or repeated exposure to substantially the same general harmful conditions." Defense is usually provided as an additional benefit under an occurrence basis policy and does not reduce the limits available to pay for a loss.

2. Claims-Made Basis

Theoretically, claims-made liability policies cover only claims actually made while the policies are in effect, regardless of when the injuries occurred. However, claims-made policies generally contain exclusions for occurrences prior to the date of inception. For a higher premium, claims-made policies can often be modified to cover "*full prior acts*." Unless renewed on a similar form with retroactive coverage or with a coverage extension known as "*extended reporting period*" or "*tail*" coverage, all coverage ends when the policy expires. Defense is frequently included within the limits of liability provided in claims-made policies and reduces the amount available to pay for a loss. With the exception of professional liability policies and high

hazard product or operations liability policies, claims made policies are rare in a real estate context. For the most part claims-made policies are manuscripted, *i.e.*, on forms drafted by the insurance company rather than ISO.

B. "Commercial" General Liability Insurance

1. Commercial versus Comprehensive General Liability

The prevalent form of general liability insurance in a commercial real estate context is commercial general liability insurance, not comprehensive general liability insurance.

2. Limits of Liability

a. Six Policy Limits

i. General Aggregate.

The "General Aggregate Limit" is the maximum the insurer is required to pay during the policy period for

- a) damages under Coverage A except bodily injury or property damage included within products-completed operations hazard,
- b) damages under Coverage B, and
- c) included expenses under Coverage C.

The General Aggregate Limit operates independently of the Products-Completed Operations Aggregate Limit.

ii. Products-Completed Operations Aggregate.

The "Products-Completed Operations Aggregate Limit" is the maximum the insurer is required to pay during the policy period for bodily injury and property damage under Coverage A included within the products-completed operations hazard. "Products-completed operations hazard" includes bodily injury and property damage occurring away from premises owned or rented by the named insured and arising out of the named insured's products or work, excluding products in the possession of the named insured, work not yet completed or abandoned, or products in transit. The Products-Completed Operations Aggregate operates independently of the General Aggregate Limit.

iii. Personal and Advertising Limit.

The "*Personal and Advertising Injury Limit*" is the maximum the insurer is required to pay under Coverage B for the damages sustained by *any one person or organization* and is subject to the General Aggregate Limit (but not the Each Occurrence Limit set forth below).

iv. Each Occurrence Limit.

The "*Each Occurrence Limit*" is the maximum the insurer is required to pay per occurrence for damages under Coverage A and medical expenses under Coverage C, subject to the General Aggregate Limit or Products-Completed Operation Aggregate Limit, as applicable.

v. Damage to Premises Rented to You Limit.

The "*Damage to Premises Rented to You Limit*" is the maximum the insurer is required to pay for damage because of property damage to any one premises while rented or temporarily occupied by the named insured, subject to the Each Occurrence Limit.

vi. Medical Expense Limit.

The "*Medical Expense Limit*" is the maximum the insurer is required to pay for medical expenses because of bodily injury sustained by any one person, subject to the Each Occurrence Limit.

[a.] Defense Costs

An ISO occurrence basis commercial general liability insurance policy states that the insurer:

"will have the right and duty to defend the insured against any 'suit' seeking those damages."

Please note that the cost of the defense is not included within the individual policy limits (except for defense of indemnitees if certain conditions are not met) and the duty to defend does not end until the insurer has:

"used up the applicable limit of insurance in the payment of judgments or settlements."

Hence, the wording of the policy does not permit the insurer to simply tender the policy limit and refuse to defend.³

[b.] Applying Limits to Separate Locations or Projects

A "*Designated Location(s) General Aggregate Limit*" (ISO form CG 25 04) endorsement to a commercial general liability policy which covers more than one location applies the General Aggregate limit separately to each location, but only with respect to bodily injury, property damage, and medical expenses. A "*Designated Construction Project(s) General Aggregate Limit*" (ISO form CG 25 03) endorsement to a contractor's commercial general liability policy which

³ Craig F. Stanovich, "Some Common Coverage Misconceptions of the CGL Policy", Expert Commentary at www.irmi.com (Jan. 2004).

covers more than one project applies the General Aggregate Limit separately to each project.

3. Injuries and Damages Covered

Commercial general liability policies are divided into three types of coverages: Coverage A relating only to "bodily injury" and "property damage," Coverage B relating to "personal and advertising injury" and Coverage C relating to "medical payments."

a. *Coverage A - Bodily Injury and Property Damage*

i. Bodily Injury.

The ISO definition of "bodily injury" is "bodily injury, sickness or disease sustained by a person, including death resulting from any of these at any time."

ii. Property Damage

The ISO definition of "property damage" is:

"physical injury to tangible property, including all resulting loss of use of that property ... or loss of use of tangible property that is not physically injured."

b. *Coverage B - Personal and Advertising Injury*

"*Personal and advertising injury*" means injury, including consequential bodily injury, arising out of one or more of the following "*offenses*":

- 1) False arrest, detention, or imprisonment;
- 2) Malicious prosecution;
- 3) The wrongful eviction from, wrongful entry into, or invasion of the right of private occupancy of a room, dwelling, or premises that a person occupies, committed by or on behalf of its owner, landlord, or lessor;
- 4) Oral or written publication, in any manner, of material that slanders or libels a person or organization or disparages a person's or organization's goods, products, or services;
- 5) Oral or written publication, in any manner, of material that violates a person's right of privacy;
- 6) The use of another's advertising idea in the insured's advertisement; or
- 7) Infringing upon another's copyright, trade dress, or slogan in the insured's advertisement.

c. *Coverage C - Medical Payments*

Coverage C requires the insurance carrier to pay medical expenses for bodily injury caused by an accident

- 1) on the premises owned or rented by the insured,
- 2) on the ways next to the owned or rented premises, or

3) because of the insured's operations.

4. Exclusions - Coverages A and B

Because different lines of insurance are designed to cover different risks and because the accurate determination of premiums depends on clearly separating the risks into categories which are subject to numerical analysis, insurance policies contain exclusions or limitations that, in effect, force the insured to purchase additional lines of insurance for excluded risks. Although several exclusions apply to Coverage A and Coverage B (e.g., willful misconduct; liquor liability; workers compensation; employers' liability; pollution; aircraft, auto or watercraft; mobile equipment; war; damage to property (subject to the exception for damage to premises rented to you); damage to your product; damage to impaired property not physically injured; recall of products, and work or property; and recording and distribution of material or information in violation of law), the exclusion most often referenced in leases is contractual liability. (Please note that in insurance jargon, if an "exclusion" applies, the named insured is not covered under the policy for damage or injury arising out of excluded risk; but if an "*exception to an exclusion*" applies, the named insured is covered under the policy for damage or injury arising out of excluded risk, but only to the extent of the exception.)

The term *contractual liability* refers to claims that arise out of contractual arrangements rather than the actions of an insured, e.g., tenant agrees to indemnify landlord against bodily injuries occurring within the premises caused by tenant's employees and customers. Coverage A in the April 2013 edition of ISO commercial general liability insurance policy contains the following exclusion from coverage:

"Bodily injury" or "property damage" for which the insured is obligated to pay damages by reason of the assumption of liability in a contract or agreement.

However, the Coverage A exclusion contains this exception:

This exclusion does not apply to liability for damages:

- (1) *That the insured would have in the absence of the contract or agreement; or*
- (2) *Assumed in a contract or agreement that is an "insured contract", provided the "bodily injury" or "property damage" occurs subsequent to the execution of the contract or agreement.*

Thus, the contractual liability provision in a commercial general liability policy will not apply to liability for bodily injury and property damages arising out of an indemnity by the named insured in a contract unless the indemnity is both enforceable and contained in an insured contract. An "insured contract" is defined, in part, as follows:

a. *A contract for a lease of premises. However, that portion of the contract for a lease of premises that indemnifies any person or organization for damage by fire to premises while rented to you or temporarily occupied by you with permission of the owner is not an "insured contract";*

...

f. *That part of any other contract or agreement pertaining to your business (including an indemnification of a municipality in connection with work performed for a municipality) under which you assume the tort liability of another party to pay for "bodily injury" or "property damage" to a third person or organization. Tort liability means a liability that would be imposed by law in the absence of any contract or agreement.*

For the purpose of leases contracts, most of the tenant's tort-related indemnities would appear to be "insured contracts." Since 1993 ISO has offered an endorsement form CG 21 39 *Contractual Liability Limitation* which redefines "Insured Contract" by deleting Subparagraph f in order to delete coverage for contractual indemnities. The insured contract exception cannot expand the scope of the commercial general liability policy beyond the coverage provided, nor does it expand the limits of liability that have been purchased. If, for example, the policy excludes coverage for property damage and bodily injury caused by pollutants, an indemnity for property damage and bodily injury caused by pollutants will not be covered even if the indemnity is contained in an insured contract and is enforceable.

Coverage B of the ISO form of commercial general liability policy a contractual liability exclusion which does not contain an insured contract exception. In order to achieve contractual liability under Coverage B, the policy must be endorsed to delete the exclusion or to include the insured contract exception. The available endorsements, e.g., ISO form CG 22 74, contain very limited coverage.

a. *Broad Form Indemnities*

Because the definition of insured contract does not exclude indemnities against bodily injury or property

damage arising from the indemnitee's own negligence, in insurance jargon, the definition covers "broad form indemnities". In 2004 ISO promulgated a new endorsement, CG 24 26, which redefined the term *insured contract* to exclude a "broad form" indemnity. The endorsement, in effect, limited contractual liability coverage to "intermediate form" indemnities which cover the contributory, but not the sole, negligence of the indemnitee. In 2013, ISO added a further limitation to pick up anti-indemnity legislation:

"However, such part of a contract or agreement shall only be considered an 'insured contract' to the extent your assumption of the tort liability is permitted by law."

b. *Defense under Contractual Liability*

The insurance company is only required "to defend the insured against any 'suit' seeking damages." Is the cost to defend an indemnitee also covered? The exception to the exclusion for contractual liability states the following with respect to the cost of defense:

Solely for the purposes of liability assumed in an "insured contract", reasonable attorney fees and necessary litigation expenses incurred by or for a party other than an insured are deemed to be damages because of "bodily injury" or "property damage", provided:

- (a) *Liability to such party for, or for the cost of, that party's defense has also been assumed in the same "insured contract"; and*
- (b) *Such attorney fees and litigation expenses are for defense of that party against a civil or alternative dispute resolution proceeding in which damages to which this insurance applies are alleged.*

Hence, in order for any defense costs incurred by indemnitor to be deemed to be damages, the indemnity must provide that defense or the cost of defense is included. But the inclusion of reasonable attorneys' fees and necessary litigation expenses within the definition of "damages" creates another problem – policy limits may be eroded. For example, if the policy has a \$1 million each occurrence limit for damages arising out of a single accident and \$500,000 is expended to pay indemnitee's "reasonable attorney fees and necessary litigation expenses," only \$500,000 will be available to pay damages to the injured party.

Is there a way that defense costs covered by the policy can be outside the policy limits and not erode the policy limits? Beginning with the 1996 edition the

Supplementary Payments – Coverages A and B section of the ISO commercial general liability insurance form, CG 00 01, was modified to include a lengthy list of conditions with respect to defense of a claim against the named insured arising from an indemnity contained in a separate contract. If all conditions in the list are not continuously met, the cost of defense of the indemnitee will be treated as damages within the policy limit, *i.e.*, costs of defense will be deducted from the proceeds available under the policy, and if the conditions are met, defense will be provided outside the limits of the policy and not reduce the policy limits. The problem is that some of the conditions are hard to comply with under any circumstances and must be met not only at the onset of the claim but also throughout the litigation as well.

C. Business Auto

"*Business auto*" (ISO Form CA 00 01) is a form of insurance covering liability arising out of the operation of automobiles by the insured. Coverage A of the ISO commercial general liability policy contains the following exclusion:

g. *Aircraft, Auto Or Watercraft*

"Bodily injury" or "property damage" arising out of the ... use ... of any ... "auto" ... Use includes operation and "loading or unloading".

11. *"Loading or unloading" means the handling of property:*

- a. *After it is moved from the place where it is accepted for movement into or onto an ... "auto";*
- b. *While it is in or on an ... "auto"; or*
- c. *While it is being moved from an ... "auto" to the place where it is finally delivered;*

but "loading or unloading" does not include the movement of property by means of a mechanical device, other than a hand truck, that is not attached to the aircraft, watercraft or "auto". (Excerpted)

Why should an owner be concerned about the auto insurance carried by a tenant or contractor? The

exposure of loading and/or unloading goods, unless being performed by use of mobile equipment (*e.g.*, forklifts), is covered by business auto insurance, not commercial general liability insurance. Business auto covers the period from the time property is moved from its original place to the time the property is finally delivered.

D. Workers Compensation / Employers Liability

1. Workers Compensation Insurance

This statutory program is a legislative compromise helping employees by imposing strict liability for injuries to the employees that occur while in the scope of employment and helping employers by imposing a schedule of maximum recoveries for injuries occurring within the scope of employment. (Please note that in this politically correct age, the name of the program is not "workmen's compensation.") If the employer does not participate in the program, the employer is penalized in two ways:

- 1) the employer is denied the common law defenses of assumed risk, negligence of fellow employees, and contributory negligence, and
- 2) there is no limit on recovery of the employee.

Although the employer must still be negligent, the likelihood of recovery by the employee is much greater. Because injuries to employees within the scope of employment are excluded from coverage of commercial general liability insurance, the judgment against the employer would not be insured. Additional insured endorsements are not available under a workers compensation or employers liability insurance policy, but waiver of subrogation endorsements are often available.

2. Employers Liability Insurance

This type of liability insurance supplements workers compensation insurance by covering the employee for bodily injury occurring while in the scope of his or her employment if the injury is not covered by workers compensation insurance. Unlike workers compensation, the injured party must prove that the employer owed a duty to the injured party, that the employer breached the duty, and that the breach was the proximate cause of the injury. Employers liability policies have defined each occurrence and aggregate limits, which limits may be expanded by an umbrella or excess liability policy.⁴

⁴ Christopher J. Boggs, *Employers' Liability Insurance – Agents Need to Know What Lawyers Already Do*, MyNewMarkets.com, August 20, 2008.

E. Umbrella / Excess Liability

Both umbrella and excess liability policies provide additional protection against catastrophic liability claims by increasing the policy limits of the primary coverages. Limits of liability are purchased in increments of \$1 million.

1. Umbrella

An umbrella liability policy has its own insuring agreement and exclusions, and usually serves three functions:

- a) Providing additional limits of liability over required limits provided by scheduled underlying primary liability policies;
- b) Providing "drop-down" coverage (*i.e.*, becomes primary) over reduced or exhausted underlying aggregate limits; and
- c) Affording coverage for claims not covered by underlying policies (if not also excluded by the umbrella liability policy) subject to a self-insured retention.

Umbrella policies do not necessarily follow the form of the underlying policies. Because both an umbrella policy and the underlying policies have their own insuring sections, differences may arise between coverages, especially if the umbrella policy and underlying policies have been issued by different companies. To ensure that no gap in coverage is created and that all insureds named in the underlying policies are picked up by the umbrella policy, the umbrella liability policy should contain an affirmative statement that the umbrella policy follows the form of the underlying policies.

2. Excess Liability

An excess liability policy relies on the underlying policy for the insuring agreement and exclusions, and provides coverage only in excess of the scheduled underlying primary liability policies. The coverage provided is usually not broader than those policies and coverage is provided only when payment has been made under a primary underlying layer.

3. Underlying Primary Liability

Both umbrella and excess liability policies contain a schedule of the underlying primary liability policies over which coverage is to be provided. This schedule will also state the amount of underlying coverage required and, where aggregate limits are provided in the primary underlying liability coverage (*e.g.*, commercial general liability coverage), that the limits must be unimpaired upon inception of coverage. It is therefore critical that umbrella/excess and general liability policies be provided with concurrent inception dates to avoid a potential gap in coverage.

F. Professional Liability

Professional liability insurance is almost invariably provided on a claims-made basis and applies only to liabilities associated with the negligence of the insured. Additional insured endorsements are not available under professional liability insurance policies.

G. Green Building Reputation Coverages

Several insurance companies are producing manuscripted "green building reputation" liability insurance policies. These policies typically have sublimits for each of their coverages. Among the coverages offered by some of these policies are the following:

- 1) the costs associated with employing a reputation management consultant to mitigate adverse publicity concerning the greenness of the building (generally 3 weeks of coverage);
- 2) reasonable adverse green claim defense costs (but insurer has no duty to defend and "reasonable" attorneys' fees, as defined, tend to be at the lower end of market rates in most major metropolitan areas);
- 3) costs of testing to determine the identity of the party that caused the problem (*i.e.*, design team, owner, contractor and/or materials manufacturer?); and
- 4) green indoor environment coverage covering bodily injury claims resulting from specialized equipment used to improve air or water quality.

Because these policies are manuscripted, coverages vary widely from company to company.

§ 10.06. CONSTRUCTION-RELATED POLICIES**A. Builders Risk**

A specialized form of *property insurance* called *builders risk* is used during the construction of a building in lieu of commercial property insurance for several reasons:

- 1) Buildings under construction are at a greater risk of damage or destruction, especially from weather;
- 2) The value of the structure varies as it is constructed;
- 3) Materials may be stored off-site or be in transit;
- 4) The ownership of portions of the building or materials may be in different parties at different points during the policy period;
- 5) The types of losses an owner incurs may be different if the building is destroyed

prior to completion, *e.g.*, liquidated damages and late delivery penalties under construction contracts and leases; and

- 6) The policy period depends on completion and cannot be fixed to a specific calendar period like the standard year used for commercial property insurance policies.

As a general rule commercial property insurance is used to cover completed buildings and builders risk insurance is used to cover buildings under construction, or, in some cases, under extensive renovation. No bright line exists as to when builders risk insurance should be used rather than commercial property insurance.

1. Policy Forms Currently Used

Although ISO has promulgated a builders risk policy form (CP 00 20), most builders risk policies are written on manuscripted inland marine forms.

2. Reporting/Non-Reporting Policy Forms

Builders risk property insurance is available in "non-reporting" (commonly known as "completed value") or "reporting" forms. Under a completed value form, coverage is automatically increased as construction occurs. A reporting form will not cover the increased value unless notice of the increase is reported to the insurance carrier.

3. Basis of Coverage (Risks Covered)

Builders risk insurance may be written on either a named peril or all risks basis, although most forms tend to be on an all risks basis. Because builders risk policies tend to be uniquely worded, one must confirm the all risks nature of each policy by checking for a statement to the effect of "covered causes of loss means risks of direct physical loss to covered property, except those causes of loss listed in the exclusions." The exclusions enumerated in an all risks builders risk policy can be numerous and include items such as the following: change of law; earthquake; flood; below surface water; governmental action; nuclear hazard; war; terrorism; consequential losses; wear and tear; settling and cracking; mechanical breakdown; changes in extreme temperatures (*i.e.*, freezing); crime; fungus; collapse; asbestos; rain, snow, ice or sleet except for interior damage; and faulty or defective planning, designs, materials, or maintenance.

4. Endorsements (or Extensions of Coverage)

Many extensions of coverage are available for builders risk insurance policies. Because manuscripted forms are generally used, these extensions may be included within the policies of some insurers, but must be added by endorsement to the policies of other insurers. Most extensions or endorsements have a "*sublimit*" which is the maximum recoverable with

respect to such extension or endorsement. Some of the extensions of coverage or endorsements which are available include the following:

- a) "Agreed value" eliminating the co-insurance provision.
- b) "Collapse" covering the damage or loss from collapse of the structure caused by certain causes of loss, generally including weight of rain, defective materials or methods of construction, and faulty design, plans, or workmanship (but almost always excludes the cost of making good or restoring defective workmanship or work which was faultily designed and of settling, cracking, shrinking or bulging of the structure);
- c) "Contract penalties" covering the contractual penalties to the insured's customers incurred as result of a delay of completion date;
- d) "Damage arising from error, omission or deficiency in construction methods, design, specifications, workmanship or materials, including collapse;"
- e) "Debris removal" covering the additional costs of removing debris resulting from a covered cause of loss;
- f) "Delay of Completion" (also known as "soft costs" or "extra expenses") covering necessary expenses incurred as result of a delay of completion date (coverage varies widely, but lenders request the inclusion of interest on the construction loan, real estate taxes, architectural and engineering supervisory costs, costs to renegotiate leases, brokerage commissions, and legal and accounting costs);
- g) "Earthquake" covering the loss or damage from earthquake, landslide, mudflow, volcanic eruption, earth sinking, rising or shifting;
- h) "Earthquake sprinkler leakage" covering damage from leaks in an automatic sprinkler system caused by earthquake or volcanic eruption;
- i) "Existing structures" covering existing building which may be undergoing renovation (in addition to the improvements being constructed);
- j) "Expediting expenses" covering the additional expenses necessarily incurred to complete construction on schedule after the occurrence of a covered cause of loss;
- k) "Flood" covering the damage or loss caused by an overflow from a stream or other body of water, surface water, waves, and tidal waves (may be required by law if the property is within a flood plain);

- l) "Freezing" covering loss caused by leaks from plumbing, heating, air-conditioning systems, or appliances (other than fire protective systems) caused by freezing;
 - m) "Governmental action" covering the damage or loss from seizure or destruction of property by order of governmental authority;
 - n) "Loss of rents" covering the loss of rents caused by delay of completion;
 - o) "Occupancy" permitting some level of occupancy of the structure under construction without termination of the policy;
 - p) "Ordinance or law" covering the increased cost of replacement resulting from the enforcement of laws or ordinances regulating repair, demolition, and reconstruction;
 - q) "Pollutant clean up and removal" covering the cost of removing pollutants released by a covered cause of loss;
 - r) "Preservation of property" covering the cost of removing covered property from the premises to preserve it from loss from a covered cause of loss;
 - s) "Property in transit" covering property while in transit to the job site;
 - t) "Property off-premises" covering property temporarily stored off the job site;
 - u) "Replacement cost, to include contractor's overhead and profit" covering the cost to repair, replace, or rebuild the damaged property, without consideration for depreciation or obsolescence, plus reasonable overhead costs including profit (subject to the policy limit);
 - v) "Scaffolding and construction forms" covering the damage to and loss of scaffolding and construction forms from a covered cost of loss;
 - w) "Sidewalks, curbs, gutters, streets, or parking lots" covering the damage to or loss of sidewalks, curbs, gutters, streets, or parking lots from a covered cause of loss;
 - x) "Testing" (sometimes called "hot and cold testing" or "mechanical breakdown") covering the damage or loss from start up or performance testing of boilers or other pressure vessels, air conditioning systems, and mechanical or electrical machines or devices;
 - y) "Theft of building materials, fixtures, machinery, equipment" covering the loss of or damage to the following by theft or attempted theft: fixtures and machinery; equipment used to service the building; and building materials and supplies used for construction;
 - z) "Trees, shrubs, plants, lawns" (sometimes called "landscaping") covering damage to or loss of trees, shrubs, plants and lawns from a covered cause of loss;
 - aa) "Site preparation costs" covering site preparation costs such as excavation, grading, and backfilling arising from a covered loss;
 - bb) "Volcanic activity" covering damage arising out of volcanic eruptions; and
 - cc) Waiver of subrogation providing that the insurer will have no rights of subrogation against named insureds, additional insureds, or any other person or entity, which the insured has waived its rights of subrogation against in writing before the time of loss
5. Property Covered
A builders risk policy usually, but not always, covers most of the property installed or intended to be installed or incidental to the structure under construction (*e.g.*, completed work, materials, supplies, fixtures, and temporary structures, *e.g.*, scaffolding), even if the property is temporary stored on-site or off-site or is in transit (other than ocean marine transit), but may sometimes not cover the following unless the policy is specifically endorsed: landscaping, construction trailers, site work (*e.g.*, grading and excavation), underground structures (*e.g.*, footings), radio antennas, equipment used to construct the building, signs, existing buildings, blueprints, and business income.
6. Amount of Recovery
Theoretically, builders risk property insurance may be written on either an actual cash value or replacement cost basis, but most policies are written on a replacement cost basis. Wording denoting replacement cost is to the effect of "the actual cost of repairing, replacing, or rebuilding the property with materials of similar kind and quality, including contractor's overhead and profit."
7. Who Purchases the Policy?
Builders risk policies may be purchased by either the owner or the general contractor. Either way, the builders risk policy for a project is a cost of construction paid by the owner. Typically, the policy is purchased by the party that can obtain the best rate. Because the owner is ultimately liable for the cost of construction (and probably personally liable under the construction loan), the owner wants to be certain that the coverage is adequate and that owner will settle any losses with the insurance carrier. The only way that contractor can avoid liability for property damage under most construction contracts is through the waiver of subrogation provision for damage covered under property insurance. Hence, the contractor is also highly motivated to have broad coverage in place and to participate in settlement discussions.

8. Parties Covered

The owner, general contractor, subcontractors and lender all have insurable interests in the construction project (see discussion on insurable interest at §10.07[E][4]), because at any given point of construction prior to completion all of these parties could have ownership of or an investment in the completed portion of the building and the materials, supplies, and other property installed or intended to be installed in the improvements under construction. Ideally, all of these parties would be "named" or "additional named insureds" (but not "additional insureds") under the policy or, in the case of the lender, "lender loss payable." Because an insured party cannot be sued by the insurer to recover the insurer's losses absent fraud by the insured party or other special circumstances, being named as insured parties has the added benefit of protecting the general contractor and subcontractors from being sued by the insurance company for property damage caused by their own negligence.

9. Policy Period

A commercial property policy is usually effective for one year. Under the builders risks policies, coverage generally begins at a stated inception date, and generally ends on the earliest to occur of the following:

- a) the interest of the insured in the property ends,
- b) the ultimate user accepts the property,
- c) *the property is put to its intended use or occupancy of any portion of the property by the ultimate user,*
- d) a fixed number of days after the project is completed,
- e) the expiration date of the policy,
- f) cancellation of the policy, or
- g) abandonment of construction.

Because builders risk property policies typically terminate coverage if any portion of the structure is occupied for purposes other than testing, a phased project (meaning most large commercial projects) will require an endorsement to permit a certain level of occupancy.

10. Protective Safeguard Warranties

"*Protective safeguard warranties*" are actually covenants by the insured which can nullify the entire builders risk policy or coverage for certain causes of loss under the policy if they are not observed. Protective safeguard warranties are typically attached by endorsement and not referenced in the declarations. The following are examples of such warranties:

- a) the building under construction must be completely fenced with at least a six-foot

cyclone fence, which must be locked during non-working hours;

- b) the building under construction must be illuminated during night hours;
- c) a working fire hydrant must be within 1,000 feet of any building under construction; and
- d) the building under construction must be under surveillance by an insured, licensed, and bonded watchperson during non-construction hours.

B. **Installation Floaters**

An "*installation floater*" is best described as a miniature builders risk policy covering one type of property (as opposed to the project) or only the work of one contractor or subcontractor. Installation floaters are property insurance. Installation floaters are typically purchased by subcontractors and written on manuscripted inland marine forms (sometimes on forms identical to builders risk forms except for the description of the property covered).

§ 10.07. PERSONS WITH INTERESTS IN INSURANCE POLICIES

A. **Named Insured**

This terminology is used for both liability policies and property policies. The *named insured* is the party who can enforce the policy. This is the party who pays the premiums and whose risk history is studied to determine the amount of premiums. The named insured also has duties under the policy; therefore, failure of the named insured to pay the premiums or to fulfill the conditions of the insurance contract could result in denial of coverage by the insurance company.

B. **Additional Named Insured**

This terminology is used for both property and liability policies. This designation is most often employed in situations in which a company is the "named insured" and its subsidiaries are "additional named insureds." An additional named insured is treated identically to the named insured, has the same duties, is subject to the same defenses, and has an obligation to pay premiums unless the policy requires that only the "first named insured" is liable for the premiums. Premiums will be adjusted to include the additional named insured's risk record.

C. **Automatic Insureds**

The term *automatic insureds* refers to certain individuals and entities that are insureds under a liability policy by virtue of the wording of coverage form. For example, ISO forms CG 00 01 or CG 00 02 contain the following automatic insureds:

(1) *If you are designated in the Declarations as:*

- (a) *An individual, you and your spouse are insureds, but only with respect to the conduct of a business of which you are the sole owner;*
- (b) *A partnership or joint venture, you are an insured. Your members, your partners, and their spouses are also insureds, but only with respect to the conduct of your business.*
- (c) *A limited liability company, you are an insured. Your members are also insureds, but only with respect to the conduct of your business. Your managers are insureds, but only with respect to their duties as your managers.*
- (d) *An organization other than a partnership, joint venture or limited liability company, you are an insured. Your "executive officers" and directors are insureds, but only with respect to their duties as your officers or directors. Your stockholders are also insureds, but only with respect to their liability as stockholders.*
- (e) *A trust, you are an insured. Your trustees are also insureds, but only with respect to their duties as trustees.*

D. Loss Payee

A *loss payee* is a party named in a loss payee endorsement. A loss payee clause is referred to as an *open clause* if the loss payee under such loss payable clause has no independent right to enforce the policy, but is simply a recipient of payments when the insured becomes entitled to collect under the policy. The drawback of an open clause is that the action or inaction of the insured can defeat the right of a loss payee to collect (*e.g.*, the insured may fail to pay premiums, make a misrepresentation, or fail to report a loss timely). On the other hand, a *closed clause* creates a separate contract between the insurer and the loss payee or mortgagee and contains language to the effect that the act or neglect of the insured will not invalidate the policy.

1. Mortgage Holders

A closed loss payee clause is also referred to as a "mortgagee clause" and provides special protections to the mortgage holder:

that payment for covered loss will be made to the mortgage holder, not to the insured or to the insured and the mortgagee; that coverage applies for the benefit of the mortgagee even if the insured's claim is denied because of the insured's acts, subject to a couple of basic requirements; and that the mortgagee will receive written notice of policy cancellation *by the insurer*. Standard mortgage holder protection *for buildings or structures only* is built into the current ISO Building and Personal Property Coverage Form (CP 00 10):

2. Loss Payable Provisions

The current edition of ISO endorsement form CP 12 18, "Loss Payable Provisions," uses four different descriptions to describe the loss payee: "Loss Payable," "Lender Loss Payable," "Contract of Sale" and "Building Owner Loss Payable." It is critical for a mortgagee to pick the right category. If "Loss Payable" is chosen in the Schedule to the endorsement, the provision becomes an open clause and the interest of loss payee is protected only if the named insured chooses to enforce the protection. However, if a "Lender Loss Payable" is chosen in the Schedule, the provision becomes a closed clause and protects a lender loss payee the same way as a mortgage holder is protected by the standard mortgage clause in the Building and Personal Property Coverage Form, with an important difference: ISO form 12 18 uses the defined term "Covered Property" *which includes both the "Building" and "Business Personal Property."* CP 12 18 may also be used by creditors whose security may be personal property, as opposed to buildings or structures, and by landlords to establish privity between the landlord and tenant's property carrier with respect to insurance proceeds payable because of the loss of landlord's property. The Building Owner Loss Payable provision states that tenant's property insurer "will adjust losses to the described building with the [landlord]" and "adjust losses to tenants' improvements and betterments with [tenant], unless the lease provides otherwise."

E. Additional Insureds

An "*additional insured*" is a party listed in the schedule of an additional insured endorsement in order to be included as an "insured" under the policy. Except as discussed in §10.07[E][4][a], the status of additional insured is almost always used for liability policies. Protection is provided to the additional insured party only to the extent stipulated in the additional insured endorsement. The policy premium is not adjusted for an additional insured's risk history. An additional insured has no obligation to pay the premium for the policy. Additional insured status for either or both of the parties to a lease, license, mortgage, or construction or

management contract is almost a universal requirement. The desired result is that the party named as "additional insured" will be protected by the liability policy of the other party independently of the indemnity and waiver provisions of the contract. However, few attorneys seem to realize that protection is provided to the insured party only to the extent stipulated in the additional insured endorsement actually used and that scores of ISO-promulgated additional insured forms with substantially different coverages exist. In addition numerous manuscripted endorsements are used.

If no particular additional insured coverage is specified in a contract, the insurance carrier is free to provide the most restrictive form. Hence, the type of additional insured endorsement required must be stipulated by ISO designation (including title, form number and edition date) or, at a minimum, described in terms of the desired coverage.

1. Advantages of Additional Insured Status

Being an additional insured under a well-written additional insured endorsement has several advantages:

- a) Additional insured status provides a safety net to the additional insured to the extent of risks covered by the named insured's policy if the indemnification provision of the contract is held to be unenforceable;
- b) The additional insured is provided direct policy rights to defense within the named insured's policy without having to depend upon indemnities and contractual liability, subject to the scope of the insurance coverage provided in the additional insured endorsement;
- c) Additional insured status may enable the additional insured to circumvent statutes prohibiting the transfer of sole negligence, *to the degree that the additional insured endorsement or statute does not exclude such*;
- d) Depending on the state, additional insured status may automatically entitle the additional insured to the excess liability or umbrella coverage of the other party because such policies frequently cover all insureds also covered under the primary liability policy; and
- e) Subrogation may be avoided, but only to the extent that coverage is provided by the additional insured endorsement.

2. Disadvantages of Additional Insured Status

However, additional insured status has several drawbacks:

- a) Each form granting coverage also restricts the coverage. Limitations of coverage added to the ISO additional insured endorsements most

commonly used in real estate transactions and construction include the following:

- 1) Exclusion of property damage or bodily injury resulting from the sole negligence or completed operations of the additional insured.
- 2) Restriction of coverage to be provided by the additional insured endorsement only to the extent permitted by law. This limitation is designed to incorporate into the policy laws enacted by states prohibiting the use of insurance to circumvent a prohibition of contractual broad form or intermediate form indemnities. For example, Section 151.104 of the Texas Insurance Code states "a provision in a construction contract that requires the purchase of additional insured coverage, or any coverage endorsement, or provision within an insurance policy providing additional insured coverage, is void and unenforceable to the extent that it requires or provides coverage the scope of which is prohibited under this subchapter for an agreement to indemnify, hold harmless, or defend."
- 3) Restriction of the breadth of the coverage afforded under the additional insured endorsement to the breadth required by the contract or agreement providing for the additional insured endorsement. Thus, if the additional insured endorsement would have covered an intermediate form indemnity, but the indemnity in the contract is a limited form indemnity, the additional insured endorsement's coverage will be restricted to a limited form indemnity.
- 4) Restriction of coverage provided under the additional insured endorsement to the lesser of the amount of insurance required under the contract or the applicable limits of the policy. For this reason, the author recommends using terminology such as "limits of at least \$_____" or "limits shall be no less than \$_____" in leases, construction contracts and other real estate-related contracts.

- b) There are numerous different forms of additional insured endorsements published by ISO and by others (usually even more restrictive than ISO forms) that are manuscripted by the insurance carriers.

- c) Additional insured endorsements do not usually include the additional insured's employees, officers, directors, contractors, or agents, as is often required by the contract (this problem may be corrected by modifying the additional insured endorsement form).
- d) The general aggregate limit of a commercial general liability policy may be impaired or exhausted if a loss is paid because of a claim against an additional insured (this problem may be corrected by application of a "Designated Location(s) General Aggregate Limit" or "Designated Construction Project(s) General Aggregate Limit" endorsement, as applicable).
- e) When liability insurance coverage is evidenced only by an ACORD™ Form 25, "Certificate of Liability Insurance," there is no guarantee of coverage (a copy of the additional insured endorsement should be obtained and carefully reviewed).
- f) For a large organization, keeping up with additional insureds may become an administrative burden, if not handled properly.

3. Specific Additional Insured Forms

a. *Additional Insured -- Owners, Lessees or Contractors*

ISO Form endorsement CG 20 10 04 13 is used in construction situations and covers only the ongoing operations of the named insured, *i.e.*, the additional insured is not covered for bodily injury or property damage arising after completion of the work. ISO Form endorsement CG 20 33 is the blanket version of ISO Form CG 20 10 and is used by larger construction companies with numerous on-going projects. The most recent edition of ISO Form endorsement CG 20 10 04 13 expressly excludes coverage for damage or injury resulting wholly (but not partially) from the act or omission of the additional insured and substitutes the word *caused* for the phrase *arising out of* to eliminate coverage for losses or injuries occurring because of contractor's operations, but not necessarily because of the contractor's actions.

b. *Additional Insured -- Owners, Lessees, or Contractors -- Completed Operations*

ISO Form endorsement CG 20 37 04 13 (see **Appendix I**) is designed to be *used in tandem with CG 20 10 or CG 20 33* in order to extend coverage for completed operations.

c. *Additional Insured -- Managers or Lessors of Premises*

ISO Form endorsement CG 20 11 04 13 does not exclude the sole or contributory negligence of landlord,

but is tied to the definition of "premises." Thus, if a lease defines "premises" in a way that excludes adjacent driveways or corridors, the landlord may not be an additional insured as to injuries occurring in the excluded areas. The endorsement also excludes occurrences after the tenant vacates. Please note that this form still uses the phrase *arising out of* rather than the word *caused*. The "arising out of" wording can be dangerous when a landlord names a tenant as an additional insured.

d. *"Blanket" Additional Insured*

If a party is using a "blanket" additional insured endorsement, the blanket nature of the endorsement does not explain its substance but, rather, that an additional insured endorsement is being applied on a blanket basis. The additional insured endorsement must be reviewed to determine its coverage. It is not uncommon for blanket additional insured endorsements to contain additional limitations or conditions, *e.g.*, reducing the policy limits available to the additional insured to the policy limits stated in the contract and specifying that the policy to which the endorsement is attached is excess, not primary, to other insurance available to the additional insured unless the contract provides to the contrary.

4. Additional Insured in a Property Insurance Context

With a few exceptions, the status of additional insured is almost always used for liability policies.

a. *Additional Insured as Their Interests May Appear*

The beneficiary of a property insurance policy must have an "insurable interest" in the insured property, *i.e.*, a lawful, substantial and enforceable interest in the safety or preservation of the subject matter of the insurance. Examples of parties having insurable interests in a building are the owner and the mortgagee. The owner is the named insured under a property policy and a lender's interest would be protected with a lender loss payable or mortgage clause endorsement. In the context of builders risk policies the terminology "additional insureds as their interests may appear" has often been used to attempt to protect parties other than the named insured and mortgagee. If the owner of a building under construction procured a builders risk policy, the owner would be the named insured and the contractor and subcontractors would be named as additional insureds as their interests may appear. However, the phrase has led to confusion in litigation and to unintended consequences. Risk managers now advise against the use of "additional insureds as their interests may appear" in builders risk policies and suggest that instead:

- 1) all parties be named as insureds under the builders risk policy, without reference to the

- phrase "additional insureds as their interests may appear",
- 2) mutual waivers of subrogation be included in the construction contracts and subcontracts, and
 - 3) the parties confirm that the policy permits the waivers of subrogation.⁵

b. Additional Insured and Mortgagees

Some lenders attempt to protect themselves by requiring that they be added as "additional insureds" in the borrowers' property policies. The problem with this approach is that there seems to be no consensus as to what the status means without further clarification by the parties. In *liability* policies and with respect to certain leasehold property policies, the relationship is spelled out by the wording of the additional insured endorsement. Similar endorsements do not exist for most *property* policies; hence, the lender is added as an "additional insured" by a general change endorsement form, often without explanation as to what the status means.

At best, it is unclear whether an additional insured status for the lender without clarification as to what the status means would either improve upon the mortgagee protections contained in a mortgagee clause or would give the mortgagee any rights in the loss adjustment process. If the mortgagee is added as an additional insured, the mortgagee should consider adding verbiage to the general change endorsement form clarifying that the additional insured status is for the purpose of allowing lender to participate in the loss adjustment process.

c. Additional Insured Status for Landlords in Property Proceeds

CP 12 19 06 07 "Additional Insured — Building Owner" provides that the building owner identified in the endorsement is a "Named Insured" with respect to the coverage provided under the tenant's property policy "for physical loss or damage to the building(s) described in the Schedule" to the endorsement.

d. Additional Insured Status for Landlords in Rental Value

CP 15 03 06 07 "Business Income — Landlord as Additional Insured (Rental Value)" provides for naming landlord as an "Additional Insured" with respect to that portion of the proceeds payable under a business income endorsement which represents the amount of rent payable under the lease. The remainder of the business income proceeds are payable to the tenant, *i.e.*, the

"Named Insured." In addition, the insurer commits to provide advance notice in writing of cancellation to the Additional Insured. This endorsement is especially useful in an absolutely net lease transaction.

5. Maintenance of Additional Insured's and Indemnitee's Own Liability Insurance

Increasingly, additional insured endorsements offered by insurers are manuscripted, company specific, and vary widely in both coverage and clarity. Evaluation of a manuscripted endorsement requires knowledge of insurance jargon and case law. Even if a party to a contract obtains indemnities and well-written additional insured endorsements for liability policies, such party should maintain its own insurance program and not rely solely on the additional insured endorsements and indemnities for several reasons:

- a) the indemnity may be held unenforceable or may not be adequately funded;
- b) the loss may not be covered by the scope of the additional insured endorsement; and
- c) the insured may have permitted its insurance policy to lapse.

6. Notice of Policy Cancellation to Additional Insureds

Most additional insured endorsements do not provide for notice of cancellation of the liability insurance policies to which the additional insured endorsements are attached. An ISO endorsement, CU 24 19, exists to provide notice of policy cancellation by the insurer to an additional insured *on an umbrella policy*. In Texas a similar ISO form, CG 02 05 entitled "Texas Changes – Amendment of Cancellation," is available for several liability policies including commercial general liability policies.

Unfortunately, similar protection does not exist for an additional insured with respect to commercial property policies. For the owner of a building that is leased under a triple net, absolutely net or bondable lease, the problem is critical because the owner is liable under the mortgage for the property, but the tenant is responsible for maintaining property insurance. If a lender loss payable clause is issued to landlord's mortgagee by the tenant's property insurance carrier, landlord's mortgagee is entitled to notice of cancellation, but the owner is not. If tenant's property insurance carrier issues a building owner loss payable clause (CP 12 18) to landlord, the clause permits the building owner to adjust losses with respect to the building (not tenant's improvements and betterments), but does not provide

⁵ Stephen A. Coombs, "Builders Risk Insurance: 'As Their Interests May Appear,'" July 2010, Expert Commentary, IRMI.com.

for notice of cancellation to landlord. If tenant's property insurance issues a an Additional Insured – Building Owner endorsement (CP 12 19) to landlord, the building owner is named as an additional insured for direct physical loss or damage to the building, but the endorsement does not provide for notice of cancellation. The best way for a landlord to protect itself is to buy the property insurance and charge the premium to the tenant; but, because of the size and creditworthiness of the typical tenant under a triple net, absolutely net or bondable lease, it is not likely that the tenant will agree. Hence, the landlord must be certain that the tenant is both creditworthy and unconditionally liable for restoring the building in the event of a casualty, whether or not insurance proceeds are available.

§ 10.08. OTHER INSURANCE

Insurance is intended to be compensatory in nature. In theory, an insured should recoup its losses but not profit from the claim. If the insured were to carry more than one policy, the insured could recover more than once and profit from a claim. Hence, the insurance industry has a series of rules concerning multiple coverages which fall under the general heading of "other insurance." By definition, a party that carries its own liability insurance and is also an additional insured under another's liability policy has multiple coverages with respect to a claim covered by the additional insured's endorsement. For this reason, an insurance provision should specify which liability insurance policy is primary, *i.e.*, must be exhausted before the other insurance policy must pay.

Another approach is to add ISO endorsement CG 20 01 which was promulgated in April 2013. The phrase "primary and noncontributory" does not appear in the ISO commercial general liability form, but is commonly required in leases, mortgages and other real estate documents. The intent of the form is not to change the substance of the policy, but to permit the phrase "primary and noncontributory" to be shown in an insurance certificate issued in connection with a transaction. The endorsement states:

The following is added to the Other Insurance Condition and supersedes any provision to the contrary:

Primary And Noncontributory Insurance

This insurance is primary to and will not seek contribution from any other insurance available to an additional insured under your policy provided that:

- (1) *The additional insured is a Named Insured under such other insurance; and*
- (2) *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.*

§ 10.09. WAIVERS OF SUBROGATION

A. Application

"Subrogation" means stepping into the shoes of another. An insurance company is subrogated to the rights of its insured against third parties in connection with a loss paid by the insurance company. The motivation for a waiver of subrogation clause is that both parties expect the insurance company to pay for the loss and not to seek to recover the amounts paid from one of the parties. If properly written, an additional insured endorsement for a liability policy makes a waiver of subrogation provision unnecessary as insurance companies usually cannot sue their own insureds (because one cannot be an additional insured under a workers compensation policy, a waiver of subrogation is always needed with respect to workers compensation insurance). Many additional insured endorsements are improperly written, restricted in coverage, or not obtained at all; hence, a waiver of subrogation is still a good idea. A waiver of subrogation can also supplement a well-written additional insured endorsement by covering liability potentially not included within the coverage of the additional insured endorsement.

B. Components of a Waiver of Subrogation Provision

A waiver of subrogation provision should contain two components:

- 1) a covenant to obtain the waiver of subrogation from the insurer, and
- 2) a release by the insured with respect to the liability which is covered by the insurance for which the waiver is sought.

The purpose of the release is to cover a situation in which the other party fails to purchase insurance or where the loss is beyond the scope or limit of the insurance policy. A release should either be general in nature or apply to the causes of loss customarily covered

by the type of insurance required to be carried by the other party, not to the insurance proceeds actually received. A release in this form protects your client against a deductible or self-insured retention under the insurance policy of the other party, for inadequate coverage by the other party, and for failure of the other party to carry insurance at all. Another method to protect your client from exposure to deductibles and self-insured retentions is to state affirmatively that the other party is to be responsible for the deductible or self-insured retention under its policy.

§ 10.10. DEDUCTIBLE VS. SELF-INSURED RETENTION

A. Deductible

Most people are familiar with how a deductible works under a property insurance policy, but a property policy is first party insurance that pays the insured for damage or loss of the insured's property. For example, if the insured's computer is stolen and the property policy has a \$250 deductible, the insurance company will pay the insured the amount of the loss minus \$250.

On the other hand, a liability policy is third party insurance, *i.e.*, the policy pays a third party that is injured by the actions of the insured. Will the insurer pay the injured party the full amount of its loss or will it pay only the amount of the loss minus the deductible? There appear to be two answers.

First, ISO endorsement form CG 03 00 "Deductible Liability Insurance" which is attached to commercial general liability insurance policies limits the obligation of the insurer to pay "only to the amount of damages in excess of any deductible amounts set forth in the" endorsement, but expressly states that the insurer's "right *and duty* to defend" is not affected by the deductible amount. The endorsement goes on to state that the insurer "may pay any part or all of the deductible amount to effect settlement of any claim or 'suit'" and that if the insurer pays, the insured will be obligated to reimburse the insurer for the deductible amount paid.

Second, according to risk managers, the insurer generally pays the full amount and then invoices the insured for the deductible. The reason for doing so is that the insurance company has the obligation to defend the claim and encounters difficulty settling the claim if it is not able to pay the total settlement amount immediately. Some insurers require security from the insured (*e.g.*, a letter of credit or cash escrow) in connection with the insured's obligation to reimburse the insurer.

B. Self-Insured Retention

Under a self-insured retention, or *SIR*, program, the insured controls the adjustment process to the extent of its self-retention either through employees or independent contractors and there is no duty on the

part of a liability insurer to defend the insured until the *SIR* is exhausted.

C. Loss Payment

Both a deductible and *SIR* require the insured to pay the first dollars of a loss.

§ 10.11. SELF-INSURANCE

The term "*self-insurance*" is an oxymoron: self-insurance is not insurance, it is the absence of insurance.

While self-insurance is an increasing commonplace practice among larger companies, there are nevertheless several dangers inherent in the practice:

- a) Insurance is governed by a well-defined body of law with respect to the insurer's obligation to defend and act in good faith, but the law applicable to normal tort litigation may not require the other party to act in good faith;
- b) The financial viability of the self-insured party cannot be independently verified;
- c) The self-insured party may not have professional staff and systems or professional outside consultants for preventing and handling claims;
- d) The self-insured party may not be able to demonstrate an acceptable loss history; and
- e) Self-insurance will not qualify as insurance in states that have anti-indemnity statutes prohibiting indemnities against a party's own negligence, but permit insurance to cover such party's negligence.

§ 10.12. QUALITY OF INSURANCE

Six services provide opinions concerning the financial strength of property and casualty insurance companies and their abilities to meet ongoing obligations to policyholders: A.M. Best Company, Standard & Poor's Insurance Rating Services, Moody's Investor Services, Fitch, Inc. (formerly, Duff & Phelps), Demotech, Inc., and Weiss Ratings, Inc. Most of the rating agencies provide rating reports on their Web sites free of charge. Rating agencies evaluate the balance sheet strength, operating performance, and business profile of insurers by focusing on factors such as claims experience, diversification of risks, reinsurance quality, expenses, sources of capital, cash surpluses and reserves, quality of assets, investment performance, liquidity, operating cash flows, profitability, yield on assets, quality of management, and years in operation. All six agencies rely on publicly available documents such as SEC and state regulatory agency filings, and all of the agencies except Weiss also rely on information

submitted to the agencies by the insurers and interviews with the insurers' managements.

A. Best's

Because A.M. Best's analysis of property and casualty insurance companies is the oldest (first published in 1900), it is generally the standard recited in real estate documents. The Property/Casualty Edition of Best's Insurance Reports evaluates approximately 3,100 property and casualty insurance companies operating in the United States against Best's qualitative and quantitative standards. A.M. Best assigns a "Financial Strength Rating" to insurance carriers. If a company is below A.M. Best's minimum asset threshold or if sufficient information is not available or is not submitted or if the insurer so requests, A.M. Best may elect not to assign a Financial Strength Rating to an insurance company.

B. Components of a Financial Strength Rating

Reports are available from the A.M. Best Web Site at no cost. Among the information contained in a report is the following:

1. "Rating"

A company is assigned one of 16 "Best's Ratings." Each rating is composed of a letter (A to F) with or without plus or minus signs. A++ is the highest rating and F is the lowest. The ratings are divided into two categories, "Secure" (A++ through B+) and "Vulnerable" (B through F).

2. "Financial Size Category"

A rated company is also assigned one of 15 "Financial Size Categories" on the basis of its capital, surplus and conditional reserve funds from which losses are paid. The Financial Size Categories are referred to as "Classes" and described with capital Roman numerals. Class I (up to \$1 million) is the smallest and Class XV (\$2 billion or more) is the largest.

3. "Outlook"

An "Outlook" indicates the potential future direction of the company's rating over a designated period of 12 to 36 months. Outlooks can be "positive," "negative," or "stable."

§ 10.13. EVIDENCING THE EXISTENCE OF COVERAGE

The most common method for evidencing the existence of coverage is to obtain a certificate of liability insurance and/or evidence of commercial property insurance. Obtaining an original policy or reviewing either an original policy or a copy of a policy is impractical, but with respect to a manuscripted policy (e.g., a builders risk policy), reviewing the original or a copy of the policy may be the only alternative. The

Association for Cooperative Operations Research and Development ("ACORD"™), a not-for-profit insurance association, publishes the standard forms of certificates of liability insurance and evidence of property insurance.

A. ACORD™ Form 25 "Certificate of Liability Insurance"

1. Disclaimers

The 2010 edition of ACORD™ 25 certificate combines all disclaimers contained in previous editions into two disclaimers located at the top of the certificate:

THIS CERTIFICATE IS ISSUED AS A MATTER OF INFORMATION ONLY AND CONFERS NO RIGHTS UPON THE CERTIFICATE HOLDER. THIS CERTIFICATE DOES NOT AFFIRMATIVELY OR NEGATIVELY AMEND, EXTEND OR ALTER THE COVERAGE AFFORDED BY THE POLICIES BELOW. THIS CERTIFICATE OF INSURANCE DOES NOT CONSTITUTE A CONTRACT BETWEEN THE ISSUING INSURER(S), AUTHORIZED REPRESENTATIVE OR PRODUCER, AND THE CERTIFICATE HOLDER.

IMPORTANT: If the certificate holder is an ADDITIONAL INSURED, the policy(ies) must be endorsed. If SUBROGATION IS WAIVED, subject to the terms and conditions of the policy, certain policies may require an endorsement. A statement on this certificate does not confer rights to the certificate holder in lieu of such endorsement(s).

Please note that the disclaimers address several matters:

- a) The certificate is issued as a matter of information only.
- b) The certificate confers no rights upon the certificate holder.
- c) The certificate does not create a contract between the certificate holder and the insurer or the insurance broker.
- d) The certificate does not amend, extend or alter the coverage afforded by the enumerated policies.
- e) If the certificate contains a statement that an insurance policy has been endorsed to include an additional insured or to include a waiver of subrogation, but the endorsements were not, in fact, issued, the holder of the certificate has no rights against the insurer or broker.

2. Subject to Policies

An ACORD™ Form 25 certificate is expressly made subject to "all terms, exclusions and conditions" of the policies listed therein, notwithstanding any requirement in any contract pursuant to which the certificate was issued. The certificate holder is also made aware that the policy limits shown in the certificate may have been reduced by paid claims.

3. Notice

An ACORD™ Form 25 certificate only requires the issuing company to deliver notice in the event of cancellation of the policies prior to the expiration date "in accordance with the policy provisions."

4. Liability Policies Only

The ACORD™ Form 25 certificate is designed to be used with liability policies. In order to utilize the form for property policies, information must be inserted into the "DESCRIPTION OF OPERATIONS / LOCATIONS / VEHICLES" space which appears below the workers compensation blank.

B. ACORD™ Form 28 "Evidence of Commercial Property Insurance"

1. Commercial Lines Policies

ACORD™ 28 is designed to summarize and state coverage under a commercial lines property policy (e.g., a commercial property policy) to a mortgagee, additional insured, or loss payee.

2. Disclaimers

The original 2003 edition of ACORD™ 28 stated:

"This is evidence that insurance as identified below has been issued, is in force, and conveys all the rights and privileges afforded under the policy";

but unlike the original 2003 edition of ACORD™ 28, the 2011 edition of ACORD™ 28 is evidence of very little. In 2006 ACORD™ issued a new edition of Form 28 inserting most of the disclaimers and limitations of the ACORD™ 25 Certificate of Liability Insurance. With the 2009 edition, ACORD™ completed the process and made the Forms 25 and 28 identical from the standpoint of disclaimers. (See §10.13[A][1] above for a discussion of the disclaimers).

3. Notice

Under the original 2003 edition of ACORD™ 28, an insurance company was required to:

"give the additional interest identified below _____ days written notice"

of termination and to send notification of changes to the policy that would affect the additional interest

"in accordance with the policy provisions or as required by law."

The 2011 edition of ACORD™ Form 28 only requires the issuing company to deliver notice in the event of cancellation of the policies prior to the expiration date "in accordance with the policy provisions."

4. Clarity

ACORD™ 28 form is designed to comply with the requirements of current lending practices and contains a much more detailed description of endorsements and coverages, including new areas of concern such as terrorism and mold.

C. Practical Considerations

1. Review Necessary

According to risk managers, the vast majority of certificates of insurance are incorrectly completed. Hence, the forms should be reviewed for accuracy.

2. Fraud

Insurance certificates are subject to fraud. A red flag is a certificate that is provided directly from the party that is supposedly insured rather than a third-party insurance agent. The recipient of a certificate may wish to consider:

- a) contacting the issuing insurance agency to confirm its existence
- b) contacting the insurance carrier to confirm the existence of the coverage, and
- c) requiring copies of all endorsements dealing with additional insureds, loss payees, mortgagees, and waivers of subrogation.

D. Texas Insurance Code, Title 10, Subtitle A, Chapter 1811 ("SB 425")

1. Approved Certificates

Texas has joined a large number of states which have enacted laws to prevent modification of the provisions of ACORD forms. Section 1810.052(b) of SB 425 provides that:

"A person may not execute, issue, or require the issuance of a certificate of insurance for risks located in this state, unless the certificate of insurance form has been filed with and approved by the [Texas Department of Insurance]."

Under Section 1810.103 of SB 425 a standard certificate of insurance form promulgated by ACORD or ISO is deemed approved when filed with the Texas Department

of Insurance, unless the standard form violates certain parameters contained in SB 425. The effect of approval of a certificate form by the Department is that a certificate only confirms that the referenced policy has been issued. Any certificate in violation of SB 425 "is void and has no effect" (Section 1811.156).

2. No Alterations or Contract References

Section 1810.103 of SB 425 prohibits any alteration or modification of a certificate of insurance form approved the Texas Department of Insurance unless the alteration or modification is approved by the Department. In addition, Section 1810.051 forbids an agent from issuing a certificate of insurance that alters, amends, or extends the coverage or terms and conditions provided by the referenced insurance policy.

"A certificate of insurance may not contain a reference to a legal or insurance requirement contained in a contract other than the underlying contract of insurance, including a contract for construction or services"

(Section 1811.154).

3. Codification of ACORD Disclaimers

In the parameters for an acceptable form, SB 425 adopts many of the disclaimers contained in ACORD forms:

"for information purposes only", the certificate "does not confer any rights or obligations other than the rights and obligations conveyed by the policy", the certificate does not convey a contractual right to a certificate holder, and "the terms of the policy control over the terms of the certificate".

4. Notice

Section 1811.155(b) prohibits any alteration in a certificate of the notice provisions of a referenced insurance policy. Under Section 1811.155(a) a certificate can require notice to a person only if the person is named in the policy or endorsement and the policy or endorsement (or law) requires notice to be provided.

5. Exception

An interesting exception to SB 425 is contained in Section 1811.002(b) with respect to certificates for property insurance required under real estate loans:

(b) This chapter may not be construed to apply to:

(1) a statement, summary, or evidence of property insurance required by a lender in a lending transaction involving:

(A) a mortgage;

(B) a lien;

(C) a deed of trust; or

(D) any other security interest in real or personal property as security for a loan;

§ 10.14. SAMPLE PROVISIONS

See **Appendices A through D** for sample provisions incorporating the principles discussed in this chapter.

APPENDIX A
LEASE INSURANCE, INDEMNITY AND WAIVER PROVISIONS

(Landlord's Form to be used in conjunction with **Appendix A**. This form assumes a multi-tenant office building, that Tenant's insurance does cover the sole negligence of Landlord within the Premises, that Chapter 151 of the Texas Insurance Code does not apply to leases although leasehold improvements may be required, and that the Lease must comply with the Texas Fair Notice Doctrine)

1. INDEMNITY.

(a) **Definitions.**

(i) "**Arising From**" means directly or indirectly, in whole or in part, (A) occurring in connection with or as a result of, (B) causing or resulting in or (C) based upon.

(ii) "**Beneficiary**" means the intended recipient of the benefits of an Indemnity or Release.

(iii) "**Claim**" means the assertion of a legal right, including, without limitation, demands or legal actions (whether filed or threatened), alleging responsibility for a Loss.

(iv) "**Indemnify**" means (A) to protect a Person against the occurrence of a Loss, including defending or contesting on behalf of a Beneficiary a Claim in litigation, arbitration, mediation, or other proceeding with counsel reasonably acceptable to the Beneficiary and paying all Legal Costs associated with such defense or contest, and/or (B) to compensate the Beneficiary for a Loss actually incurred.

(v) The "**Landlord-related Persons**" are

(A) Landlord;

(B) Property Manager;

(C) Landlord's Mortgagee(s);

(D) any affiliates or subsidiaries of the Persons enumerated in items (A) through (C); and

(E) all of the officers, directors, employees, shareholders, members, partners, agents and contractors of the Persons enumerated in items (A) through (D) .

(vi) "**Legal Costs**" means court costs, attorneys' fees, experts' fees or other expenses incurred in investigating, preparing, prosecuting or settling any legal or alternative dispute resolution action or proceeding.

(vii) "**Loss**" means any actual or alleged liability, cost or expense (including Legal Costs), loss, damage (including actual, consequential, and punitive), hurt, judgment, or penalty of whatever nature or description, incurred by a Person or property, including, without limitation, (i) harm to or impairment, loss, or diminution in the value of tangible or intangible property or its use, including, without limitation, loss of business or revenues, (ii) physical harm to or death of a natural Person, or (iii) "personal and advertising injury" as such term or terms are defined by the edition of ISO form CG 00 01 in effect on the date of this Lease.

(viii) "**Parties**" means Landlord and Tenant.

(ix) "**Person**" means a natural person, a trust or estate, or a corporation, partnership, limited liability company or other form of entity.

(x) The "**Tenant-related Persons**" are Tenant and its shareholders, members, managers, partners, directors, officers, employees, agents, contractors, sublessees, licensees and invitees.

(xi) "**Release**" means to relinquish a Claim and/or to release a Beneficiary from liability for a Loss actually incurred.

(b) **Scope of Indemnities and Releases.** All Indemnities and Releases in this Lease:

(i) are independent of, and will not be limited by,

(A) each other;

(B) any insurance obligations in this Lease (whether or not complied with); or

(C) any one-action rule under workers compensation laws, and

(ii) will survive the Expiration Date until all related Claims against the Beneficiaries are fully and finally barred by Applicable Law.

All Applicable Law affecting the validity or enforceability of any Indemnity or Release contained in this Lease is made a part of such provision and will operate to amend such Indemnity or Release to the minimum extent necessary to bring the provision into conformity with Applicable Law and cause the provision, as modified, to continue in full force and effect. **ALL INDEMNITIES AND RELEASES IN PARAGRAPH 1(b) WILL BE ENFORCED TO THE FULLEST EXTENT PERMITTED BY APPLICABLE LAW FOR THE BENEFIT OF THE BENEFICIARY THEREOF, EVEN IF THE APPLICABLE CLAIM IS CAUSED BY THE ACTIVE OR PASSIVE, JOINT, CONCURRENT OR COMPARATIVE NEGLIGENCE OF SUCH BENEFICIARY, AND REGARDLESS OF WHETHER LIABILITY WITHOUT FAULT OR STRICT LIABILITY IS IMPOSED UPON OR ALLEGED AGAINST THE BENEFICIARY, BUT WILL NOT BE ENFORCED TO THE EXTENT THAT A COURT OF**

COMPETENT JURISDICTION HOLDS IN A FINAL JUDGMENT THAT A LOSS IS CAUSED BY THE WILLFUL MISCONDUCT OR GROSS NEGLIGENCE OF THE BENEFICIARY.

(c) **Indemnity.** Tenant will Indemnify the Landlord-related Persons against, all Claims Arising, or alleged to Arise, From any Loss;

(i) suffered by a Tenant-related Person or any other Person which occurs in the Premises;

(ii) caused by a Tenant-related Person which occurs outside the Premises;

(iii) [add others as appropriate, e.g., default, mechanics' liens, violations of law and hazardous materials contamination].

(d) **Waiver of Subrogation.** Landlord and Tenant Release against each other all Claims for Losses Arising, or alleged to Arise, From damage to or loss of the Project, Premises, furniture, fixtures or equipment or other personal property, (including loss of business or revenues), that are covered by the Releasing Party's property insurance or that would have been covered by the Required Insurance Policies if the Releasing Party fails to maintain the property coverages required by this Lease. The Party incurring the Loss will be responsible for any deductible or self-insured retention under its property insurance. Each Party will notify the property insurance companies issuing its property policies of the Release set forth in this paragraph and will have the property insurance policies endorsed, if necessary, to prevent invalidation of coverage. This Release will not apply if it invalidates the property insurance coverage of the releasing Party. **THE RELEASE IN THIS PARAGRAPH WILL APPLY EVEN IF THE DAMAGE OR LOSS IS CAUSED IN WHOLE OR IN PART BY THE NEGLIGENCE OR STRICT LIABILITY OF THE RELEASED PARTY, BUT WILL NOT APPLY TO THE EXTENT THE DAMAGE OR LOSS IS CAUSED BY THE GROSS NEGLIGENCE OR WILLFUL MISCONDUCT OF THE RELEASED PARTY.**

2. TENANT'S INSURANCE.

(a) **Required Policies.** Tenant will, at its sole expense, procure and maintain the insurance coverages set forth in **Appendix B**, having limits no less than the amounts set forth in **Appendix B**. Tenant will, at its sole cost and expense, comply with such requirements during the Term of the Lease.

(b) **Minimum Requirements.** The coverages set forth in **Appendix B** are minimum requirements and not a determination as to all of the insurance coverages or maximum amount of insurance to be provided by Tenant. The failure of Landlord to demand full compliance by Tenant with respect to the minimum coverages outlined in **Appendix B** will not constitute a waiver by Landlord with respect to Tenant's obligation to maintain such coverages. Tenant will purchase such other insurance policies and/or endorsements or increase the policy limits of any policy set forth on **Appendix B**, if required by any Landlord's Mortgagee.

(c) **Special Remedy.** Tenant's failure to obtain and maintain the required insurance will constitute a material breach of, and default under, this Lease. If Tenant fails to remedy such breach within 5 days after notice from Landlord, Landlord may, in addition to any other remedy available to Landlord, at Landlord's option, purchase such insurance, at Tenant's expense. Tenant will Indemnify the Landlord-related Persons against any Claims Arising From Tenant's failure to purchase and/or maintain the insurance coverages required by this Lease.

APPENDIX B
TENANT'S INSURANCE

(Landlord's Form to be used in conjunction with **Appendix A**)

1. Specific Requirements.

INSURANCE	COVERAGES NO LESS THAN	OTHER REQUIREMENTS
Workers Compensation	Statutory Limits	
Employers Liability	\$1,000,000 each accident for bodily injury by accident/each employee for bodily injury by disease/ bodily injury by disease for entire policy	
Commercial General Liability (Occurrence Basis)	\$1,000,000 per occurrence \$2,000,000 general aggregate \$2,000,000 product-completed operations aggregate limit	<ol style="list-style-type: none"> 1. Most current edition of Insurance Services Office, Inc. ("ISO") form CG 00 01, or equivalent. 2. Designated Location(s) General Aggregate Limit endorsement (Most current edition of ISO form CA 25 04, or equivalent). 3. Contractual liability under Coverage A to respond to a broad form indemnity. 4. Current edition of ISO form CG 20 01, or equivalent.
Business Auto Liability (Occurrence Basis)	\$2,000,000 combined single limit	<ol style="list-style-type: none"> 1. Most current edition of ISO form CA 00 01, or equivalent. 2. Includes liability arising out of operation of all owned, hired and non-owned vehicles.
Umbrella Liability (Occurrence Basis)	\$5,000,000	<ol style="list-style-type: none"> 1. Written on an umbrella basis in excess over and no less broad than the liability coverages referenced above. 2. Inception and expiration dates will be the same as commercial general liability insurance. 3. Must contain follow form language. 4. Coverage must "drop down" for exhausted aggregate limits under commercial general liability insurance.
Commercial Property	100% replacement cost of all of Tenant's furniture, fixtures and equipment and any non-Building Standard leasehold improvements	<ol style="list-style-type: none"> 1. Causes of Loss-Special Form (formerly "all risk"), most current edition of ISO form CP 10 30. 2. Waiver of subrogation in favor of Landlord-related Persons. 3. Landlord to be named Building Owner Loss Payable on most current edition of ISO form CP 12 18. 4. Landlord to be named Additional Insured -- Building Owner on most current edition of ISO form CP 12 19.
Business Income and Extra Expense Coverage	No less than 6 months of income and ongoing expenses.	<ol style="list-style-type: none"> 1. Waiver of subrogation in favor of Landlord-related Persons. 2. Endorsement to cover losses arising from interruption of utilities outside the Premises (ISO Form CP 15 45). 3. Landlord to be named as Additional Insured on most current edition of ISO form CP 15 03.

2. General Insurance Requirements.

(a) **Policies.** All policies must

(i) Be issued by carriers having a Best's Rating of A or better, and a Best's Financial Size Category of Class X, or better, and authorized to sell insurance in the State in which the Building is located;

(ii) Be endorsed to be primary with the policies of all Landlord-related Persons being excess, secondary and noncontributing;

(iii) Be endorsed to provide a waiver of subrogation in favor of the Landlord-related Persons;

(iv) With respect to all liability policies except workers compensation/employers liability, be endorsed to include the Landlord-related Persons as "additional insureds" (The additional insured status under the commercial general liability policy will be provided on the most current edition of ISO form CG 20 11, or equivalent);

(v) Contain a provision for 30 days' prior written notice by insurance carrier to Landlord required for cancellation, nonrenewal, or substantial modification; and

(b) Limits, Deductibles and Retentions

(i) Except as expressly provided above, no deductible or self-insured retention in excess of \$25,000 without the prior written approval of Landlord.

(ii) No policy may include an endorsement restricting, limiting or excluding coverage in any manner without the prior written approval of Landlord.

(c) Forms

(i) If the forms of policies, endorsements, certificates, or evidence of insurance required by this *Appendix* are superseded or discontinued, Landlord will have the right to require other equivalent forms; and

(ii) Any policy or endorsement form other than a form specified in this *Appendix* must be approved in advance by Landlord.

(d) Evidence of Insurance. Insurance must be evidenced as follows:

(i) ACORD™ Form 25 *Certificates of Liability Insurance* for liability coverages;

(ii) ACORD™ Form 28 *Evidence of Property Insurance* for property coverages;

(iii) Evidence to be delivered to Landlord prior to commencing operations at the Property and at least 30 days prior to the expiration of current policies; and

(iv) ACORD™ forms must

(A) Show the Landlord-related Persons as certificate holders (with Landlord's mailing address);

(B) Show Tenant as the "Named Insured;";

(C) Show the insurance companies producing each coverage and the policy number and policy date of each coverage;

(D) Name the producer of the certificate (with correct address and telephone number) and have the signature of the authorized representative of the producer;

(E) Specify the additional insured status and/or waivers of subrogation;

(F) State the amounts of all deductibles and self-insured retentions;

(G) Show the primary status and aggregate limit per project where required; and

(H) Be accompanied by copies of all required additional insured endorsements.

(e) **Copies of Policies.** If requested in writing by Landlord, Tenant will provide to Landlord a certified copy of any or all insurance policies or endorsements required by this Contract.

APPENDIX C
CONSTRUCTION CONTRACT INSURANCE, INDEMNITY AND WAIVER PROVISIONS

[Note: **This form assumes that the Contractor is carrying the builders risk insurance, if required, and that Chapter 151 of the Texas Insurance Code applies**]

3. Indemnities and Releases.

(a) **Definitions.**

(i) "**Arising From**" means directly or indirectly, in whole or in part, (A) occurring in connection with or as a result of, (B) causing or resulting in or (C) based upon.

(ii) "**Beneficiary**" means the intended recipient of the benefits of an Indemnity or Release.

(iii) "**Claim**" means the assertion of a legal right, including, without limitation, demands or legal actions (whether filed or threatened), alleging responsibility for a Loss.

(iv) The "**Contractor-related Persons**" The "Contractor-related Persons" are (A) Contractor, (B) all Subcontractors and other Persons involved in performance of the Work that are required by this Contract to be managed or supervised by Contractor, (C) the shareholders, members, managers, partners and Affiliates of the Persons described in items (A) and (B), and (D) the officers, managers, directors, employees and agents of the Persons described in items (A) through (C).

(v) "**Indemnify**" means (A) to protect a Person against the occurrence of a Loss, including defending or contesting on behalf of a Beneficiary a Claim in litigation, arbitration, mediation, or other proceeding with counsel reasonably acceptable to the Beneficiary and paying all Legal Costs associated with such defense or contest, and/or (B) to compensate the Beneficiary for a Loss actually incurred.

(vi) The "**Owner Parties**" are (A) Owner, (B) any lender whose loan is secured by a lien against the Property, (C) any ground lessor of the Property; (D) Owner's Representative, (E) the respective shareholders, members, partners, managers, beneficial owners, and Affiliates of the Persons described in items (A) through (D), and (F) any officers, managers, directors, Affiliates, employees and agents of the Persons described in items (A) through (E).

(vii) "**Legal Costs**" means court costs, attorneys' fees, experts' fees or other expenses incurred in investigating, preparing, prosecuting or settling any legal or alternative dispute resolution action or proceeding.

(viii) "**Loss**" means any actual or alleged liability, cost or expense (including Legal Costs), loss, damage (including actual, consequential, and punitive), hurt, judgment, or penalty of whatever nature or description, incurred by a Person or property, including, without limitation, (i) harm to or impairment, loss, or diminution in the value of tangible or intangible property or its use, including, without limitation, loss of business or revenues, (ii) physical harm to or death of a natural Person, or (iii) "personal and advertising injury" as such term or terms are defined by the edition of ISO form CG 00 01 in effect on the date of this Lease.

(ix) "**Parties**" means Owner and Contractor.

(x) "**Person**" means a natural person, a trust or estate, or a corporation, partnership, limited liability company or other form of entity.

(xi) "**Release**" means to relinquish a Claim and/or to release a Beneficiary a Loss actually incurred.

(b) **Scope of Indemnities and Releases.** All Indemnities and Releases in this Lease:

(i) are independent of, and will not be limited by,

(A) each other;

- (B) any insurance obligations in this Contract (whether or not complied with);
- (C) any prohibitions against Indemnifying joint tortfeasors under comparative negligence statutes; or
- (D) any one-action rule under workers compensation laws, and

(ii) will survive the completion of the Work until all related Claims against the Beneficiaries are fully and finally barred by Applicable Law.

All Applicable Law affecting the validity or enforceability of any Indemnity or Release contained in this Contract is made a part of such provision and will operate to amend such Indemnity or Release to the minimum extent necessary to bring the provision into conformity with Applicable Law and cause the provision, as modified, to continue in full force and effect.

(c) **Indemnities.** Contractor will Indemnify the Landlord-related Persons against all Claims Arising, or alleged to Arise, From any of the following:

- (i) any Contractor-related Persons' acts or omissions, including the ongoing or completed operations of Contractor-related Persons, negligence, fraud, breach of fiduciary duty, or willful, reckless, or criminal misconduct;
- (ii) any default by Contractor or any Subcontractor under this Contract;
- (iii) any defect in the Work, equipment, or materials,
- (iv) any failure by Contractor or any Subcontractor to maintain the Required Insurance Policies;
- (v) any violation of or failure to comply with Applicable Law by a Contractor-related Person;
- (vi) any release or disturbance of Hazardous Materials that occurs in or from the Property and Arises From a Contractor-related Person's activities or operations or the remediation of such release or disturbance.

(d) Contractor will Indemnify the Owner-related Persons, against all Claims and Losses arising out of or resulting from bodily injury to, or sickness, disease or death of, any employee, agent or representative of Contractor or any of its subcontractors, regardless of whether such Claim or Loss Arises From, or is alleged to Arise From, in whole or in part, the negligence of any Owner-related Person, **IT BEING THE EXPRESSED INTENT OF OWNER AND CONTRACTOR THAT IN SUCH EVENT THE CONTRACTOR IS TO INDEMNIFY THE OWNER-RELATED PERSONS FROM THE CONSEQUENCES OF THEIR OWN NEGLIGENCE**, whether it is or is alleged to be the sole or concurring cause of the bodily injury, sickness, disease or death of Contractor's employee or the employee of any of its subcontractors. The indemnity under this Paragraph will not be limited by any limitation on the amount or type of damages, compensation or benefits payable by or for Contractor under workers compensation acts, disability benefit acts or other employee benefit acts.

(e) **Waiver of Subrogation.** Contractor and Owner Release each other and any Mortgagee from all Claims for Losses Arising, or alleged to Arise, From damage to the improvements under construction, damage to or loss of fixtures or materials, equipment or other personal property within the Job Site including loss of business or revenues, that are covered by the Releasing Party's property insurance or that would have been covered by the Required Insurance Policies if the Releasing Party fails to maintain the property coverages required by this Contract. The Party incurring the damage or loss will be responsible for any deductible or self-insured retention under its property insurance. Each Party will notify the property insurance companies issuing its property policies of the Release set forth in this paragraph and will have the property insurance policies endorsed, if necessary, to prevent invalidation of coverage. This Release will not apply if it invalidates the property insurance coverage of the releasing Party. **THE RELEASE IN THIS PARAGRAPH WILL APPLY EVEN IF THE DAMAGE OR LOSS IS CAUSED IN WHOLE OR IN PART BY THE NEGLIGENCE OR STRICT LIABILITY OF THE RELEASED PARTY, BUT WILL NOT APPLY TO THE EXTENT THE DAMAGE OR LOSS IS CAUSED BY THE GROSS NEGLIGENCE OR WILLFUL MISCONDUCT OF THE RELEASED PARTY.**

4. **Insurance.** Contractor will continuously maintain in force all of the minimum insurance coverages set forth in **Appendix D** ("**Required Insurance Policies**") during the period beginning on the date this Contract becomes effective and ending on the later to occur of the date Contractor receives the Final Payment or the last day any Contractor-related Person is physically present on the Property (whether or not this Contract has ended). If required by any mortgagee of the Property, Contractor will procure additional insurance coverages, obtain other endorsements and/or increase the limit of any Required Policy. The coverages set forth in **Appendix D** are minimum requirements and not a determination as to all of the insurance coverages or maximum amount of insurance to be provided by Tenant.

APPENDIX D
CONTRACTOR'S INSURANCE

1. Specific Requirements.

INSURANCE	COVERAGES/LIMITS NO LESS THAN	OTHER REQUIREMENTS
Workers compensation	Statutory Limits	
Employers Liability	\$1,000,000 each accident for bodily injury by accident/each employee for bodily injury by disease/ bodily injury by disease for entire policy	
Commercial General Liability (Occurrence Basis)	\$_____ per occurrence \$_____ general aggregate \$_____ product-completed operations aggregate limit \$_____ personal and advertising injury limit	<ol style="list-style-type: none"> 1. Current edition of ISO form CG 00 01, or equivalent. 2. Designated Construction Project(s) General Aggregate Limits (current edition of ISO CG 25 03), or equivalent. 3. Contractual liability under Coverage A to respond to a broad form indemnity. 4. This insurance will be maintained in identical coverage, form and amount, including required endorsements, for at least 2 years following the date of final completion of construction 5. Current edition of ISO form CG 20 01, or equivalent.
Contractors Pollution Liability	\$_____ per occurrence \$_____ aggregate	<ol style="list-style-type: none"> 1. Having a 5-year extended reporting period, if written on a claims-made basis.
Professional Liability	\$_____	<ol style="list-style-type: none"> 1. Maintain for a period of not less than 2 years after completion of construction
Business Auto Liability (Occurrence Basis)	\$_____	<ol style="list-style-type: none"> 1. Current edition of ISO form CA 00 01, or equivalent 2. Includes liability arising out of operation of all owned, hired and non-owned vehicles.
Umbrella Liability (Occurrence Basis)	\$_____	<ol style="list-style-type: none"> 1. Written on an umbrella basis in excess over and no less broad than the liability coverages referenced above. 2. Same inception and expiration dates as commercial general liability insurance, or contain a non-concurrency endorsement. 3. Coverage must "drop down" for exhausted aggregate limits under the liability coverages referenced above.
Contractors Equipment	Actual cash value of all of Contractor's equipment and other property	Definition of Covered Property broad enough to cover tools and spare parts and property in transit or stored off-site.

INSURANCE	COVERAGES/LIMITS NO LESS THAN	OTHER REQUIREMENTS
Builders Risk Property Insurance (on an all risks basis)	1. Coverage on a completed value basis. 2. Amount of coverage: initial Contract Sum, plus \$_____, subject to subsequent modification of Contract Price 3. Property covered: <ul style="list-style-type: none"> • Entire Work at Job Site • All structures under construction • All property on the Job Site for installation, including materials and supplies • All property at other locations but intended for use at the Job Site, including materials and supplies • All property in transit to the Job Site, including materials and supplies • All temporary structures at the Job Site, including scaffolding, falsework and temporary buildings 	1. <u>Required endorsements</u> <u>Minimum Sublimit</u> Additional expenses due to delay in completion \$ _____ Business income/rental value \$ _____ Agreed penalty \$ _____ Damage arising from error, omission, or deficiency in design, specifications, workmanship or materials, including collapse No Sublimit Debris removal additional limit \$1,000,000 Earthquake \$ _____ Earthquake sprinkler leakage \$ _____ Expediting expenses \$ _____ Flood \$ _____ Freezing \$ _____ Ordinance or law No Sublimit Pollutant clean up and removal \$ _____ Preservation of property No Sublimit Replacement cost No Sublimit Testing No Sublimit 2. No protective safeguard warranties permitted. 3. Occupancy of up to ____% of covered property to be permitted. 4. Deductibles will not exceed the following: All risks of direct damage, per Occurrence: \$5,000 Delayed opening waiting period: 5 days Flood, per occurrence: \$25,000, or excess of NFIP if in flood zone A Earthquake and earthquake sprinkler leakage, per occurrence: \$25,000 5. Name Owner's construction lender as "mortgagee" or "lender loss payable" in a mortgagee clause acceptable to such lender

2. General Requirements.

(a) **Policies.** All policies must

(i) Be issued by carriers having a Best's Rating of A or better, and a Best's Financial Size Category of Class X, or better, and authorized to sell insurance in the State in which the Work is located;

(ii) Be endorsed to be primary with the policies of all Owner-related Persons being excess, secondary and noncontributing;

(iii) Be endorsed to provide a waiver of subrogation in favor of the Owner-related Persons;

(iv) With respect to all liability policies except workers compensation/employers liability, be endorsed to include the Owner-related Persons as "additional insureds" (The additional insured status under the commercial general liability policy will be provided on ISO forms CG 20 10 and CG 20 37, in tandem);

(v) Contain a provision for 30 days' prior written notice by insurance carrier to Owner required for cancellation, nonrenewal, or substantial modification; and

(b) **Limits, Deductibles and Retentions**

(i) Except as expressly provided above, no deductible or self-insured retention in excess of \$25,000 without the prior written approval of Owner.

(ii) No policy may include an endorsement restricting, limiting or excluding coverage in any manner without the prior written approval of Owner.

(c) **Forms**

(i) If the forms of policies, endorsements, certificates, or evidence of insurance required by this Appendix are superseded or discontinued, Owner will have the right to require other equivalent forms; and

(ii) Any policy or endorsement form other than a form specified in this Appendix must be approved in advance by Owner.

(d) **Evidence of Insurance.** Insurance must be evidenced as follows:

(i) ACORD™ Form 25 *Certificates of Liability Insurance* for liability coverages;

(ii) ACORD™ Form 28 *Evidence of Commercial Property Insurance* for property coverages;

(iii) Evidence to be delivered to Owner prior to commencing operations at the Property and at least 30 days prior to the expiration of current policies; and

(iv) ACORD™ forms must

(A) Show the Owner-related Persons as certificate holders (with Owner's mailing address);

(B) Show Contractor as the "Named Insured;"

(C) Show the insurance companies producing each coverage and the policy number and policy date of each coverage;

(D) Name the producer of the certificate (with correct address and telephone number) and have the signature of the authorized representative of the producer;

(E) Specify the additional insured status and/or waivers of subrogation;

(F) State the amounts of all deductibles and self-insured retentions;

(G) Show the primary status and aggregate limit per project where required; and

(H) **Be accompanied by copies of all required additional insured endorsements.**

(e) **Copies of Policies.** If requested in writing by Owner, Contractor will provide to Owner a certified copy of any or all insurance policies or endorsements required by this Contract.

