Drafting Insurance Requirements Provisions in Leases, Contracts, and Real Estate Documents

What You Don't Know Can Hurt You

By Michael S. Hale

Fast Facts

Many insurance requirements provisions in contracts, leases, and real estate documents do not adequately cover client exposures attempting to be addressed by the drafter attorney.

Recent updates in certificates of insurance being used to evidence coverage present substantial issues for drafters of contracts and leases.

Sometimes attorneys are expected to be all things to all people. As stalwarts for protecting clients, they often are expected to have uncanny knowledge of other industries such as property and casualty insurance. This is no easy feat; it takes a seasoned insurance broker or underwriter to understand the ever-changing policy contracts and available endorsements that limit or expand available coverage. Certificates of insurance only make this process more complex, particularly in light of new forms that do not require notice of cancellation to an additional insured. Many businesses and their attorneys put far too much stock in certificates over the policies themselves.

Attorneys often default to template insurance requirements provisions that could be outdated and expose the client to either uncovered loss or breach of contract for not providing the agreed-upon coverage.

This article provides guidelines for attorneys involved in drafting and negotiating insurance requirements provisions in contracts, leases, or mortgage documents.

Basic Insurance Issues Facing Drafters of Contracts, Leases, and Mortgage Documents

1. **Many insurance requirements provisions include outdated terms such as "comprehensive general liability insurance" or "public liability insurance," which are, generally speaking, no longer commonly used in the insurance industry.** Instead, "commercial general liability insurance" is used to refer to liability insurance for bodily injury, property damage, and defined personal and advertising injury.

2. **The term "personal injury" in a commercial general liability insurance policy does not mean bodily injury.** Instead, it means non-bodily injury such as slander, libel, defamation, invasion of privacy, wrongful eviction, and sometimes non-employment discrimination.

3. **Michigan law requires courts to interpret the contract as a whole.**[1] However, it is generally a good idea to have all insurance requirements in one section. Although some template provisions will include an indemnity section under "Insurance," it is usually better to keep the insurance requirements section separate from the indemnity provision to avoid unintended interpretations.

4. **Ambiguities are construed against the drafter, but this might be negotiable.** For example, some businesses include language indicating that the usual rule of *contra proferentum* does not apply and the parties have jointly drafted the language. For less-experienced parties, the drafter should exercise particular caution to either define words with specific intended meaning or be prepared to accept the plain and commonly understood meaning, particularly when dealing with insurance terms.

5. **Attorneys may have concerns about holding themselves out as insurance experts when they are not.** It is advisable to defer to the client's insurance agent to review such provisions before they are signed by the parties to the contract, or to recommend separate insurance counsel. Too often, insurance agents only receive copies of *executed* agreements when not much can usually be offered to address issues that may exist.

6. **Certificates of insurance should, for most purposes, be assumed to have little effect.** Not only do these certificates say they are for information only and do not change the policy, but they are almost always drafted by insurance agents who are legal agents of the policyholder and not the insurer. Thus, the certificates are not likely binding on many insurers, who are quick to ask agents not to even send them copies. Therefore, treat certificates of insurance as suspect and obtain and review the actual policy or endorsement.

   Under relatively recent changes, all state insurance departments have accepted the Acord 25 Certificate of Insurance, which replaces an older version. This new certificate includes no representation that the insurer (or agent) will provide any notice to a listed additional insured. This presents major concerns when representing landlords who may be allowing tenants to insure the building, who now also may receive no notice of cancellation or change in coverage. These issues also apply in other contracts such as purchase agreements. As a result, it is best to obtain a copy of an actual endorsement from the insurer confirming the additional insured status, which also provides a notice of cancellation provision in that endorsement.

   Notably, mortgagees are usually covered by the property insurance policy protecting the real property collateral. This may not, however, be the case concerning business inventory lien holders.

   In light of the above, be very cautious when counseling a client regarding agreeing to language that requires notification of cancellation to the other party.

7. **The contractual liability insurance coverage for indemnity obligations is frequently overlooked in insurance requirements provisions, and this could mean disaster for both parties.** It is advisable to include a sentence requiring contractual liability insurance in the commercial general liability insurance policy. However, keep in mind when drafting the provision that such coverage is often less broad than the contractual indemnity provision itself.

8. **There are more than 30 different types of additional insured endorsements available on a standard commercial general liability insurance policy.**[2] This includes additional insured club members, charitable institutions, volunteers, executors, administrators, and lessors, among others. Which endorsement is right for your client? It is wise to seek the advice of the client's insurance broker and outside insurance counsel.

9. **"Primary and noncontributory" additional insured language in a contract's insurance provisions can be important to the additional insured but warrants caution.** Many commercial general liability insurance policies do not automatically contain language purporting to elevate the additional insured to primary status on the named insured's policy. An endorsement is typically required. If this is the case, a copy of that endorsement should be obtained by the additional insured.

10. **"Blanket" additional insured endorsements may extend limited coverage but should not always be relied on.** There is an endorsement available on the commercial general liability insurance policies of many insurers that will provide "automatic" additional insured status if required by a written

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contract including a lease. However, such endorsements can sometimes limit coverage in certain ways, such as excluding coverage for renovations or improvements made to real estate. As a result, when representing the additional insured, attempt to have the party listed specifically by endorsement.

11. **Avoid allowing another party to provide the property insurance coverage for your client.** For example, in a triple net lease, some landlords require that the tenant insure the landlord's building. This is a recipe for complete disaster from both parties' perspectives. Not only is the landlord allowing the tenant and its insurance agent to protect the assets of the landlord, it also opens itself up to inferior coverage as a loss payee and the potential of not being notified in the event of a cancellation.

12. **Additional insureds do not have the same rights as named insureds.** For example, even though a landlord may be listed as an additional insured on the other party's liability insurance policy, this coverage is only derivative of the negligence of the named insured tenant. It is critical, therefore, that the landlord continues to maintain its own liability coverage as lessor regardless of the insurance maintained by the tenant.

13. **Waivers of subrogation are common in lease agreements but are frequently overbroad in scope.** These waivers are designed to legally block the other party's insurer from pursuing it in a reimbursement action but should be limited to waiving the rights of the insurer to subrogate for covered claims and avoid including other liability-limiting provisions.

14. **Automobile exposures are often given inadequate attention in insurance requirements provisions.** All businesses, including tenants, have automobile exposures. Require additional insured status on these policies.

15. **Workers' compensation exposures are often given inadequate attention in insurance requirements.** Attempt to negotiate a waiver of subrogation in favor of your client on the other party's workers' compensation policy. For example, if a tenant's employee suffers an injury on your client's premises, you would want to try to block the tenant's workers' compensation carrier from attempting to subrogate against your landlord client.

16. **In purchase agreements, clearly define when the risk of loss transfers.** Coordinate this with appropriate insurance coverage for the client.

17. **Requirements to name additional insureds should not apply to all the defined policies.** This is a common mistake. Workers' compensation, for example, is not a policy on which an additional insured can be listed.

18. **If your client agrees to name a company and its "employees, officers, agents, and members" in the contract, know that this is not automatic.** The insurer will typically list only the company without the other individuals.

19. **Be cautious about professional liability insurance policies and additional insureds.** Professional liability policies, also known as errors and omissions policies, are frequently included in the insurance requirements provisions of professional service contracts, such as the hiring of an IT or staffing company. Be particularly careful about requiring additional insured status of your client on a professional liability policy because it usually means that coverage for lawsuits by your client against the hired company would be barred under the insured-versus-insured exclusion, which is almost always contained in such policies.

Conclusion

If your head is spinning after reading the above, you are not alone. Further, this is only the tip of the iceberg on insurance-related issues your clients may face. Many attorneys, understandably, are not insurance experts and do not clearly comprehend the nature of what should be included in insurance requirements provisions or how to best protect their clients through adequate insurance policies. It is advisable to consult competent insurance agents and insurance counsel in these evaluations. ■

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ENDNOTES

1. *Auto-Owners Ins Co v Churchman*, 440 Mich 560; 489 NW2d 431 (1992).
2. See Insurance Services Office, Inc <http://www.iso.com/> (accessed September 12, 2013).