

CGL—Fire Legal

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Although it sounds like a television drama in which a powerful lawyer from a massive city law firm fights for truth and justice by day and is a heroic firefighter by night, fire legal is a reference to a slightly less exciting insurance coverage buried within the guts of the commercial general liability (CGL) policy.

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Struggling for its identity and rightful place among other insurance coverage, fire legal has taken the path of many a struggling actor—including changing names. Formerly known as Fire Legal Liability Coverage—Real Property (as included within the Broad Form Comprehensive General Liability Endorsement GL 04 04), the 1986 commercial general liability policy shortened its moniker to fire damage. A rather substantial makeover was undertaken and unveiled in the July 1998 CGL: a new name—Damage to Premises Rented to You—and a new look (complete with enhancements).

Contributing to its obscurity is the fact that, unlike other coverage, such as personal and advertising injury or medical payments coverage, there is no express coverage grant for Damage to Premises Rented to You. Except for being displayed with a limit on the Declarations Page, Damage to Premises Rented to You is mentioned only twice in passing in the December 2004 CGL form—once as an exception to certain property damage exclusions and once under the Limits Section. In other words, something you might not notice unless you were looking for it.

Despite its journeyman status, Damage to Premises Rented to You coverage may be important, particularly if you or your client need it. Immediately after a loss is usually too late, so let's take a look at this.

Girl Power

Your client, Girl Power Equipment Repair, Inc., has built a successful power equipment maintenance and repair business which she has operated out of her garage for the past several years. Since demand continues to rise for her services (from people like me who can't find the oil plug on their lawnmower), she decides to rent one of four service bays from a service garage on Main Street. The landlord has her sign the "boilerplate" 3-year lease (more on that later). She then moves in, lock, stock, and barrel (at least stock).

After a close call with some spilled gasoline, she asks if her insurance will cover her if she damages the landlord's property. You immediately think "Fire Legal." But what do you tell her? Best answer at this point, "I'll call you right back."

Damage to Property—Exclusions

This is what you dreaded—now you have to read her policy. Girl Power Equipment Repair, Inc., has purchased from you a December 2004 CGL policy with no endorsements. A quick look at the Declarations Page causes a mild panic—you can't even find Fire Legal.

Then you thumb through the CGL policy form and come across Exclusion j. (1.), which eliminates coverage for damage to property Girl Power Equipment owns, rents, or occupies. Seemingly, she has no coverage for damage to the landlord's property because she definitely rents and occupies the bay in which she is repairing equipment.

But wait! You read on and find a paragraph that looks to be stuck in as an afterthought. The paragraph is at the end of Coverage A—Exclusions and says exclusions c. through n. (you're pretty sure exclusion j. falls between c. and n.) does NOT apply to damage by fire to premises while rented to or temporarily occupied by the named insured with the permission of the owner. Also, reference is made in the paragraph to application of a separate limit.

And then you remember the reference to a separate limit is a reference to the Damage to Premises Rented to You Limit, which for Girl Power is shown on the Declarations Page as \$50,000—any one premises. This is what used to be called Fire Legal (or something like that).

Damage to Premises Rented to You

Back to Girl Power's question: Does her insurance cover damage to her landlord's property? Nothing fosters confidence like the answer you are about to give her—it depends!

Damage by Fire

You see that the Damage to Premises Rented to You coverage provided by the exception is very limited—coverage applies only if the damage is caused by *fire*. So if the gasoline spill resulted in fire, she would be covered for damage caused by the fire to the landlord's premises (up to \$50,000). But what about water damage to the walls and floors that resulted when a faucet was left running all night? She would have no coverage for the water damage. As the damage is not by fire, the Damage to Premises Rented to You *exception* does not apply—and thus exclusion j. eliminates coverage (even though Girl Power is likely liable).

Damage to Premises

The building in which Girl Power is a tenant is a large, relatively new building with a value of about \$400,000. The other tenants also have significant amounts of contents, mostly inventory, stored in their portions of the premises, with total values of about \$500,000.

When you discover this, you begin to wonder if \$50,000 is enough "fire legal" coverage. What if the fire spreads beyond Girl Powers' premises and causes damage to other portions of the building and the inventory of the other tenants?

Should you recommend Girl Power increase the Damage to Premises Rented to You limit to \$400,000 (the value of the building)? Or maybe even \$900,000 (the total value of the building and the other tenants' inventory)? What about the possible loss of use claim on top of direct damage? Maybe you should recommend a limit for Damage to Premises Rented to You of \$1 million or more!

While it is important to periodically reconsider the reasonableness of limits purchased by your client, here you are missing an important point. In our situation, Damage to Premises Rented to You coverage applies only to damage *to the premises*. In other words, coverage applies only to *that portion of the real estate* owned by the landlord *and* rented by Girl Power—which is about one quarter of the building (one of four bays).

Each Occurrence Limit

If a fire does spread to other portions of the building or damages the property of other tenants, Damage to Premises Rented to You coverage does not apply. Does that mean Girl Power has no insurance for such damage? No!

Since the other portions of the building are not rented to or occupied by Girl Power, exclusion j. does not apply. Nor does exclusion j. apply to the contents of the other tenants (presuming the contents are not in Girl Power's custody or control). In either case, the Each Occurrence Limit (less any amounts paid under Damage to Premises Rented to You for the same occurrence) is available to pay damage for which Girl Power is legally liable.

New Limit

Now that you know what is and what is not covered by Damage to Premises Rented to You coverage, you can make a better recommendation as to a limit. Considering the building value is \$400,000 and we occupy about one quarter of the building, a limit of \$100,000 for Damage to Premises Rented to You coverage seems reasonable. Armed with your new knowledge, you now meet with Girl Power and dazzle them with your expertise, culminating in your well-reasoned recommendation to increase the Damage to Premises to You Limit from \$50,000 to \$100,000.

Damage Other Than by Fire

When you deftly explain all of this to Girl Power, they are duly impressed, increase their Damage to Premises Rented to You limit as you have recommended, but remain concerned—what if they are liable for damage to the landlord's property but the cause is *not fire*? Some eyebrows were raised when you used the faucet/water damage example. Can they get insurance for damage other than fire?

You get back to the office and leaf through your handy-dandy forms book, but can't seem to find a CGL endorsement that fits. And that's because, although it is actually a liability form, the endorsement you are looking for is found within the *Commercial Property Forms*—the Legal Liability Coverage Form CP 00 40 04 02.

Legal Liability Coverage Form

This form provides coverage for damage to tangible property of others (including loss of use of the damaged property) that is in Girl Power's care, custody, or control and described in the Declarations. A separate limit, which applies on a per accident basis, applies in the Commercial Property Policy to the Legal Liability Coverage Form. This form must be combined with other commercial property forms, such as a Causes of Loss Form, to provide complete coverage terms. Expressly eliminated is coverage for damage to electronic data.

The Trigger

To trigger the Legal Liability Coverage Form, Girl Power must, because of an accident, be legally obligated to pay for the damage to the property and the cause of damage must be included in the Cause of Loss Form attached. If the Causes of Loss—Special form is selected, Girl Power would have coverage for damage to the landlord's property for a wide array of causes IF they are legally liable for the damage. Now, water damage to the landlord's property caused by Girl Power's forgetting to shut off the faucet is covered.

Recommendation Accepted

Girl Power understands your recommendation and agrees to purchase the Legal Liability Coverage Form, describing the property to which this coverage applies as the building located on Main Street, and listing the limit as \$100,000. Girl Power purchases the Legal Liability Coverage Form as an endorsement to their commercial property policy. This coverage is in addition to the CGL's Damage to Premises Rented to You limit of \$100,000.

The Seminar

Girl Powers' business is going swimmingly. In fact, because of the growth of the business, Girl Power takes over the entire building on Main Street (all four bays) and is the only tenant (the landlord rewrites the lease for Girl Power). Dutifully, you keep abreast of these changes and increase the Legal Liability Coverage Form limit from \$100,000 to \$400,000 (the full value of the building) to reflect the increased space now rented to Girl Power.

Girl Power services are so popular that they have begun offering full day seminars at local hotels, attracting over 100 prospects and customers to each session. The typical arrangement is for Girl Power to rent the hotel room for 1 day, with the rental including use of the hotel's audio-visual equipment (projector, screen, microphone, etc.) as well as tables (including table linens) and chairs for the seminar.

Sprinkler Discharge

At one seminar, the projector is not properly handled by Girl Power, resulting in the equipment overheating, which in turn sets off the sprinkler system within the room rented by Girl Power. The water from the sprinkler discharge damages the hotel's wall coverings, carpeting, chandelier, tables, chairs, and screen—total damage is estimated at \$5,000.

The hotel sends a bill to Girl Power for \$5,000, asserting Girl Power's negligence in handling the equipment is the direct cause of the damage, and therefore, Girl Power is legally liable to pay the \$5,000. Girl Power sends along the claim to you, including the bill, and requests coverage under her Legal Liability Coverage Form.

Bad News and Good News

The insurance company providing Girl Power their commercial property policy, the Legal Liability Coverage Form in particular, denies coverage for this accident. The reason—the only property described on the Legal Liability Coverage Form is the building located on Main Street. As the hotel was not listed on the Declarations, no coverage applies to that location. Does Girl Power have an uninsured loss?

Damage to Premises Rented to You

Recall that you have continued coverage under Girl Power's CGL for Damage to Premises Rented to You with a limit of \$100,000. But wasn't that coverage for damage by fire only?

July, 1998 Enhancement

In addition to the paragraph you found at the end of the Coverage A—Exclusions that granted an exception for damage to premises by fire, beginning in July of 1998, the commercial general liability policy grants a second exception to Exclusion j., Damage to Property.

Immediately following Exclusion j. (6) is an exception that provides coverage for the very loss Girl Power has just suffered. The exception specifically states that paragraphs (1), (3), and (4) of Exclusion j. do not apply to property damage to premises, *including the contents of the premises*, rented to a named insured (Girl Power) for a period of *7 or fewer consecutive days*, for any cause of damage *other than fire*. Of course, an insured must be legally obligated to pay for such damage to trigger this coverage exception and any payments made under this exception are subject to the Damage to Premises Rented to You limit.

Since the \$5,000 loss to Girl Power is the result of their negligence, the rental of the premises was for only 1 day (7 or fewer consecutive days) and the cause of the damage was water (not fire), coverage does apply to the entire loss—both the real property (wall coverings, carpet, chandelier, etc.), and the personal property (screen, tables, chairs, etc.) that has been damaged. As the loss falls squarely within the coverage exception, Girl Power has coverage for their \$5,000 property damage loss.

But what if the above loss was the result of a fire and not a sprinkler discharge, you ask? Excellent question! The answer is coverage would still apply—but only to damage to the premises itself (wall coverings, carpet, and chandelier) and not to damaged personal property (screen, tables, chairs, etc.). Of course, a solution is to amend the Legal Liability Coverage Form to describe the hotel seminar operations and locations in the Declarations, thereby providing broader coverage for Girl Power for their seminars.

The Risk Management Consultant

After the sprinkler discharge loss at the hotel (and the insurance company's denial of coverage), Girl Power engages an independent risk management consultant to analyze and evaluate the risks confronting Girl Power with respect to their potential for liability for the property of others. Among other things, the risk management consultant obtains a copy of Girl Power's real estate lease on Main Street.

The real estate lease has one sentence that you just know is going to cause a problem:

- Tenant agrees to pay for any damage to the demised premises, regardless of cause.

Contractual Liability Exclusions

Surely your exemplary handling of Girl Power's insurance, including their purchase of the Legal Liability Coverage Form with a \$400,000 limit, should take care of this situation. But, unfortunately, it may not.

A special exclusion is added to the Causes of Loss—Special Form that applies when the Legal Liability Coverage Form is attached. Exclusion (2) (a) is entitled Contractual Liability and states in part:

- We will not defend any claim or 'suit,' or pay damages that you are legally liable to pay, solely by reason of your assumption of liability in a contract or agreement.

Where does this leave us? Coverage will still apply *if* Girl Power would be liable for damages *absent their agreement to be responsible*. For example, the faucet running all night that causes water damage would likely be negligence of Girl Power, who would be liable for the resulting damage even if no lease wording existed. However, what if the building is destroyed by lightning? Girl Power is liable, but their liability is *solely because of the lease agreement*.

The contractual liability exclusion would most likely eliminate coverage for damage that is beyond the control of Girl Power (yet, they have agreed to pay for such damage).

Commercial General Liability—Contractual Liability

What about the contractual liability coverage in the CGL policy? Doesn't the definition of "insured contract" include a contract for a lease of premises? It most certainly does, but also contains a very important limitation.

Explicitly eliminated from "insured contract" is any portion of a contract for lease of premises that indemnifies any person or organization for damage by fire to the premises while rented to or temporarily occupied by the named insured. In short, the CGL does little to help Girl Power for damage to the premises for which they would not otherwise have liability.

Commercial Property Insurance: Suggested Solutions

If the lease is already in place, the landlord may not be willing to amend the lease to remove Girl Power's responsibility to pay for any damage to the building. Given the situation, you probably should be thinking about recommending to Girl Power that they remove the Legal Liability Coverage Form applicable to their Main Street location and to purchase Building and Personal Property Coverage Form (CP 00 10 04 02), listing Building Coverage for Main Street reflecting the value of the building (\$400,000) and attaching the Causes of Loss—Special Form.

Insurable Interest

It is possible for the insurance company to resist providing this property coverage for Girl Power, the tenant, for a building Girl Power does not own. The objection may be based on lack of "insurable interest" grounds.

As Girl Power has agreed to be responsible and will suffer financial loss if the building is damaged or destroyed, it is generally undisputed that Girl Power, despite not having an ownership interest, does have an insurable interest in the building. An alternative, however, may be to write the policy for Girl Power and add the landlord as a loss payee.

Amending the Lease

It is possible (maybe even likely) that the landlord already has purchased property insurance that protects the building if damaged by certain causes of loss. For the tenant to also purchase coverage on the same building may be redundant and certainly appears to be a poor use of assets. When this issue is brought to the landlord's attention, the landlord may be willing to amend the lease and remove the portion which holds the tenant (Girl Power) completely responsible for all damage to the building.

In fact, if you have your druthers, you would ask the landlord to consider the following:

- It is agreed that the tenant is not be responsible for any damage to the premises.

The above would have the effect of relieving the tenant of liability for damage to the building, no matter how caused, obviating the need for Girl Power to purchase commercial property coverage, legal liability coverage form, at least for their premises on Main Street.

An alternative may be a *mutual* waiver of recovery rights, which may read as follows:

- It is agreed that the tenant and landlord waive all rights of recovery against the other for damage to property and neither is responsible to the other for damage to property.

A third alternative may be wording in which the release is tied to insurance recovery. The phrase may read:

- To extent the landlord can collect the proceeds of landlord's insurance, it is agreed that landlord waives rights of recovery against tenant for damage to the landlord's property.

For all of the above, it is important for you to know that such waivers or releases of liability are allowed under the standard Commercial Property Conditions (CP 00 90 07 88) provided the releases or waivers are in writing and executed prior to a loss.

Conclusion

Those policyholders who lease or rent space are presented with exposures that may not be properly handled by standard "fire legal" or "damage to premises rented to you" coverage found in the CGL. Reviewing the real estate lease terms is critical to properly identifying and managing the risk, whether treatment of risk is by insurance, non-insurance risk transfer (the lease agreement), or a combination of both techniques. In any event, understanding the limitations of insurance, such as the contractual exclusion in the legal liability coverage form, is a must in managing your client's real estate risks.

The preceding is not to be considered the rendering of legal, accounting or professional services. All references to suggested lease wording or amendments are for illustrative purposes ONLY and are not intended to be nor should be construed as advice on non-insurance risk transfer.

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