Real Estate: Contractual Liability

Owners or Managers of Real Estate

Could this happen to you?

• A visitor arrives at an apartment complex to pick up his fiance’ (a resident) for a date. As the couple is leaving, they are confronted by a group of individuals in a common area and the visitor is shot. The shooter was never identified and no arrests were ever made. The victim files suit against the apartment owner alleging inadequate security, noting that the complex is in a high-crime area. The plaintiff argues that the owner failed to exercise reasonable care for the safety of tenants and invitees.

• A vehicle jumps a curb, leaps across the sidewalk adjacent to a building and crashes into the waiting room of a medical clinic in a strip mall, which is owned and managed by the insured. Some of the individuals in the waiting room are killed; several others are severely injured. The plaintiffs, surviving family members and the injured bring suit alleging that the owner of the strip mall breached the expected duty of care owed to tenants and invitees in the design of the parking lot and strip mall.

• At a high-end condominium complex, an inebriated guest of a condominium owner decides to ride the valet parking “lift,” which is essentially a moving ladder that takes the valet staff from one level of the parking garage to another quickly. The guest falls from the lift into the lift pit, suffering severe bodily injury, including brain damage and paralysis. The plaintiff files suit against a number of defendants, including the building owner. The plaintiff alleges that the building owner breached the duty of care owed to tenants and invitees with respect to the parking lift.

• During a building renovation process, an elevator maintenance company is brought in to repair the elevator. The repair requires a scaffold to be built inside the elevator shaft to support two workers who are completing the repair. During the repair, the scaffold collapses and both workers fall approximately 30 feet to the bottom of the shaft. One worker dies from his injuries, and the other is severely injured, including brain injuries. Both families of the workers sue the building owner, the contractor and the company that provided the lumber for the scaffold. The final settlement totals $17.5 million, with the building owner paying $2 million of that loss.

All of the loss scenarios above demonstrate the importance of contractual risk transfer provisions in contracts. All property owners or managers can better protect themselves against potential losses by using appropriate contractual risk-transfer mechanisms. A properly written and reviewed contract can help to reduce the cost of a claim and perhaps prevent your company from paying unnecessarily for disputes and claims that may be caused by third parties, tenants or subcontractors.
Below are a number of issues relating to contractual liability and how to better manage this exposure as an owner or manager of real estate. As with any legal matter, you should consult with your own legal counsel prior to entering into any contract.

**Contractual Risk Transfer**

For the building owner or manager, contracts with numerous entities are a normal part of the business process. Some common contracts related to real estate include:

- Property Management
- Elevators
- Escalators
- Snow Removal Contract
- Janitorial and General Maintenance
- Lease Agreements (Owner and Tenant)
- Security
- Landscaping
- Pool Service/Maintenance
- Fitness Center Service/Maintenance

Contractual risk transfer is the process of shifting responsibility for loss or damage arising from the performance of a contract from one party to another. It does not absolve transferors from liability, but it gives transferees another source of funding from which to pay a loss, other than their insurance policy or their own assets. In addition, contractual risk transfer provisions can:

- Assist in placing liability where it should rest—with the party performing or responsible for the service.
- Provide certainty amongst contractual parties.
- Encourage safe practices—if a service provides or tenants know they will be held financially responsible for an accident, they will generally pay more attention to safe practices.

Transferring risk, however, is not as simple as executing a contract that specifies the duties or services to be performed. A contractual promise is only as good as the person or entity making the promise. Because of the large dollar losses that can occur, the person or entity should provide evidence of insurance, generally done with a certificate of insurance, that spells out:

- The limits of available insurance for the operation that is being performed.
- The insurance company providing the particular insurance coverages.
- Who is named as an Additional Insured for the contracted services.

Being added as an additional insured to a contractor’s or tenant’s insurance policy allows for direct rights of recovery under that insurance policy. The insurance policy should include the duty to defend the additional insured, so that the expenses of any lawsuits insured under the policy go against the contractor’s or tenant’s insurance policy, not the additional insured’s policy.

It’s also important to remember to obtain certificates of insurance from any third parties or subcontractors that a contractor or tenant might be engaging to perform services that support the contractor’s or tenant’s operations. This provides further assurance of adequate funds to pay for losses if the cause of the loss is due to the activities of the third party.

**Indemnification/Hold Harmless**

Having “hold harmless” wording in a contract can be a great tool in transferring risk to the party that is performing a service. In turn, having it in a contract where you are the provider of services can be a very serious matter. An indemnification/hold harmless agreement is a provision in which the indemnitee agrees to “indemnify and hold harmless” the indemnitor against certain liabilities arising out of the activity that is the subject of the contract.

However, the hold harmless agreement is only as good as the available funds to pay or defend claims. Thus, obtaining a certificate of insurance that shows adequate limits of insurance is still critical to this process.

**Waiver of Subrogation**

Often, when there is a claim, the building owner’s insurance policy may initially pay the claim to avoid additional legal issues and costs that can be incurred by delaying payment to the injured party. However, the building owner’s insurance company may then attempt to recover that payment from any other liable party, including tenants, contractors or subcontractors.

Subrogation allows an insurer that has paid a claim to look to other potentially liable entities for contribution to cover all or part of a loss. However, if an insured “waives” its right of subrogation against another in a contract, it would deprive the insurer from subrogating against the other liable party.

In turn, a building owner should look to include a waiver of subrogation in its favor in any contract with a party that provides the owner with additional insured status or hold harmless indemnification. By doing this, the building owner will be protected from claims by the third party’s insurer.
**Contract Liability “Best Practices” for Owners or Managers of Real Estate**

Below are some items to consider when entering into contracts concerning your buildings and properties. While not all-inclusive, it provides a good starting point to help avoid future problems.

- Require that legal counsel review all contracts, including lease and service agreements.
- Whenever possible, use a standard contract rather than a special or manuscripted contract.
- Gain insurance protection by having yourself added to a contractor’s or tenant’s insurance policy as an additional insured. Verify that the insurance coverages include workers compensation, general liability and umbrella insurance, where applicable.
- Review the contract to ensure that there is “indemnification/hold harmless” wording in your favor within the contract.
- Do not waive your right of subrogation with any of your contracted service providers.
- Obtain certificates of insurance to confirm adherence to contractual requirements. Verify that the limits provided on the certificates meet or exceed your own insurance limits and that the insurance company providing the limits is rated a minimum of “A-“ by A.M. Best Company, a leading insurance rating firm.
- Maintain a file of all certificates of insurance received from third parties. Review the file on a monthly basis to determine which certificates are in need of updating. Make providing a current certificate of insurance a contract provision.
- Confirm that certificates of insurance are received from all third-party vendors.
- Require contractors to be responsible for all subcontractors, including making sure that insurance specifications and insurance limits are adequate. Require contractors to work safely and maintain safe workplaces.
- Where permissible, contracts should have a provision requiring that the contractor’s or tenant’s insurance is primary and the building owner’s is excess.

---

**For More Information**

Contractual liability can pose a serious exposure for commercial real estate owners. For additional information about Chubb’s loss prevention guidance for real estate companies, please contact your Chubb-appointed agent or broker.
Chubb Group of Insurance Companies | www.chubb.com