



CAMBRIDGE

PROPERTY & CASUALTY
SPECIAL REPORT

OVER 100 INSURANCE “GOTCHA’S” THAT CAN RUIN YOUR DAY (OR BUSINESS OR PERSONAL ASSETS)

This Special Report was written by Kenneth R. Hale, J.D., CPCU, AAI, LIC. Mr. Hale is Chairman of Cambridge Property & Casualty and an attorney licensed to practice law in the State of Michigan. He can be contacted at 734-525-2412 or khale@cambridge-pc.com. More Special Reports are available at www.cambridge-pc.com.

INSURANCE CARRIERS ARE NOT THE ENEMY.

Insurance carriers pay more in claims and expenses than they receive in premiums.

The intention of this report is not to demean insurance carriers. They serve society quite well, paying billions of dollars in claims every year. In the aggregate, property and casualty insurance carriers in the 2009 calendar year received \$423,900,000,000 in premiums and paid \$427,715,000,000 in expenses and claims before investment income. This is about \$1.01 paid for every dollar received.

YET MANY POLICYHOLDERS ARE NOT PAID IN FULL OR NOT PAID AT ALL.

The problem is not that insurance carriers are not paying claims; it is that many policyholders are not being paid because their policy was not property negotiated.

- Insurance policies are written by lawyers for lawyers, and most insureds are not lawyers.
 - Insurance policies are precisely written using, in most cases, basic policy forms that must be endorsed to meet the needs of the insurer and the insured. (Some basic forms are broader than others.)
 - Insurance carriers add endorsements to the basic policy in order to modify the basic policy form to meet its need to avoid unacceptable operations or exposures. These are typically exclusions that limit what coverage is available under the basic policy.
 - On the other hand, insureds want to add endorsements to expand coverage to meet their particular needs. The problem here is that insureds do not know what endorsements to ask for.
 - By and large our experience is that insurance companies (with some exceptions) do not go out of their way to deny claims; however, if the plain language of the insurance policy indicates that a
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claim is not covered or that a policy condition has not been met, the insurance adjuster is likely required to deny the claim.

- Insurance agents, according to the Michigan Supreme Court, are in most cases “order-takers,” and are not required to counsel you or walk you through the complexities of an insurance policy and to advise you of your options to add endorsements or to use broader policies to begin with. Agents usually focus on price because this is what we ask them to do.
- Both insureds and agents are worried about the wrong things, and they make a decision based on price rather than terms and conditions.
- This leaves the typical insurance policy purchaser thinking that their insurance policy will provide protection for an uncovered event that could put an insured out of business or cost them their personal assets.
- Insureds are expected by the courts to read policies (*Zaremba Equipment v Harco National Insurance Co.*), but we all know that we don't. Even if we did, we still would not know about the hundreds or thousands of options available by way of endorsements to the basic policy that would avoid claim “gotcha's,” meaning reasons for an insurance claims adjuster to deny a claim.

THREE MAJOR REQUIREMENTS TO SUCCESSFUL AND PROMPT CLAIM PAYMENTS.

- Insurance company ability to pay. (Is it solvent?)
- Insurance company obligation to pay. (The insurance company is obligated to do what the four corners of the policy say.)
- Insurance company willingness to pay promptly and without litigation. (This involves the insurance company's philosophy and reputation for either finding a way to pay or a way to deny claims.)
- It also involves the insurance company's relationship with you and your agent, and your ability to provide detailed and accurate information to support your claim.

MAJOR CLAIM GOTCHA'S.

The purpose of this Special Report is to alert policyholders to the major issues that impact the obligation and willingness of an insurance company to pay claims. Policyholders need to be alert to these insurance “gotcha's” before a loss occurs. (This document is general in nature and may not apply in all situations. Individual consultation should be obtained on your specific insurance and risk management needs. In addition, while we refer to “standard forms,” there can be a variety of “standard forms.”)

**IMPORTANT: COMMERCIAL INSURANCE POLICIES ARE NEGOTIABLE
IN PRICE, TERMS AND CONDITIONS.**

GENERAL GOTCHA'S

Gotcha #1

My claim was denied. I sued my insurance company, and the court said that I had an obligation to read my policy.

- What you had last year with another insurance carrier does not count.
 - What you thought was covered does not count.
 - What you hoped was covered does not count.
 - What your agent said was covered does not count.
 - A brochure does not count.
 - A summary from your agent does not count.
 - **The only thing that counts is the four corners of the insurance policy as set forth in the policy and endorsements.**
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Gotcha #2

My claim was denied. It turns out that it had a new exclusion that I never had before.

- You chose the lowest premiums over better terms and conditions (or fewer “gotcha’s”).
 - Do not give up a lot to save a little.
 - We train our insurance agents to worry about the wrong thing, which is price, when we should insist that the focus be first on the terms and conditions necessary to protect our assets and only then price.
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Gotcha #3

My agent completed an application that was not accurate or complete, and the insurance company denied my claim based on misrepresentation. I never saw the application.

GENERAL GOTCHA'S

- Inaccurate applications can cause a coverage denial later. For example, if you said that the building was 70% occupied and it was actually 70% vacant, you will have a problem.
- Accuracy and completeness of information are essential.
- If an agent completes an application, it is binding on you in Michigan even if you did not sign it or see it. This is because the agent is legally your agent.
- ACORD applications are the standard application universally used by insurance companies. It is virtually impossible to completely answer these applications without making misrepresentations.

These are just a few of the questions on the standard application:

- Any exposure to flammables, explosives, chemicals? *(Everyone has flammables and chemicals of some sort.)*
- Any catastrophe exposure? *(Wouldn't a building fire be a catastrophe?)*
- Any policy or coverage declined, cancelled or non-renewed during the prior three years? *(Typically, only your agent knows if an insurance carrier declined your account.)*
- Any uncorrected fire code violations? *(Does this mean that you have not complied with the building codes or that you have been cited?)*
- Any past, present or discontinued operations involving storing, treating, discharging, applying, disposing or transporting of hazardous material? *(Even light industrial operations and offices have waste. How is "hazardous" defined?)*
- Any employees under 16 or over 60 years of age? *(Almost every business would have to say yes to this one.)*
- Any seasonal employees? *(Is the college student in the summer seasonal?)*
- Any employees with physical handicaps? *(We all have some physical handicaps, whatever that means.)*
- Any employees traveling out of state? *(Most employers have employees that may travel infrequently out of the state.)*
- Any athletic team sponsored? *(Many employers send a check to help out a church or other team. Does this constitute sponsorship?)*
- Any hold harmless agreements? *(Every insured has these in almost every agreement they execute.)*

GENERAL GOTCHA'S

- Any vehicles used by family members? (*Does this mean once a year when I loan my car to my wife?*)
- List underlying insurance coverage information (include all restrictions). (*You would have to copy every insurance policy.*)
- List laser endorsements. (*Does an insured know what this is?*)
- Any subrogation waivers or extensions of coverage? (*Again, you will have to copy and attach every policy you have in place.*)
- Give details of all liability claims exceeding \$10,000 or occurrences that may give rise to claims during the past 5 years, whether insured or not. (*Would you even know what occurrences may give rise to a claim?*)
- The incomplete or inaccurate answers to these and other application questions could be the cause for a claim denial or policy rescission.
- Answer ambiguously if necessary when it is impossible to answer a question yes or no. For example, the answer should be “always possible” to the question “any employees with physical handicaps?” (What is a “physical handicap” anyway?)

Gotcha #4

I changed insurance companies, and the policy was cancelled within 30 days after they inspected my business. My prior insurance company will not take me back, and now I have to pay a significantly higher premium elsewhere.

- Commercial insurance policies can be cancelled by the insurance company without any reason with 10 to 30 days notice.
- There are many risks in changing insurance carriers. Do so carefully.
- These risks include:
 - More limiting terms and conditions than you had before.
 - Different classifications and rates imposed after the policy expires because of audits.
 - After an inspection, the new insurance company imposes expensive loss prevention requirements.
 - After an inspection, the insurance company can cancel you midterm.

GENERAL GOTCHA'S

Gotcha #5

I thought that a complaint to the state regulatory authorities would get my claim paid. It didn't work and was a waste of my time.

- State officials cannot change policy language or make an insurance company pay if it is not a covered claim.
 - The complaint statistics, however, are interesting. Go to www.michigan.gov/DLEG and search "Insurance Company Complaint Statistics."
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Gotcha #6

My insurance company became insolvent, and it looks like my current or future claims will not be paid.

- You purchased a policy based on the lowest premium without examining the ability of the insurance company to pay a claim on a long term basis.
- A start is to check the carrier's A.M. Best rating. Carrier ratings are:
 - A++, A+ = Superior
 - A, A- = Excellent
 - B++, B+ = Good
 - B, B- = Fair
 - C++, C+ = Marginal
 - C, C- = Weak

This is not a guarantee, however. Even A rated insurance companies can rapidly become insolvent.

- If an insurance company is consistently the most competitive, it is doing so in order to gain premium dollars that can be invested. These investments will hopefully cover underwriting losses. This is called cash flow underwriting. This can cause an insurance company to become insolvent when investment income fails to cover underwriting losses.
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GENERAL GOTCHA'S

- There are many examples of cash flow insurance companies that have failed. Let's take a look at just one example: Kemper Insurance Company.

A.M. Best's Rating	
1999 – A	3/3/03 – B+
7/3/00 – A	3/3/03 – B
5/7/02 – A-	5/1/03 – C++
12/24/02 – B+	6/10/03 – D

Note the six month span from an A- to a B+ rating. The B+ rating is the beginning of the end for most insurance carriers because mortgage companies will not accept less than A- ratings. When this happens, policies are placed elsewhere, leaving the accounts that could not be placed elsewhere still insured. This is called “adverse selection” and leads to a fast downward spiral.

- This is cash flow underwriting using Kemper as the example:

Year	Premiums	Underwriting Income or Loss	Investment Income	Difference
1998	\$2,853,056,000	-\$208,762,000	+\$356,091,000	+\$147,329,000
1999	\$2,430,695,000	-\$263,158,000	+\$308,913,000	+\$45,755,000
2000	\$2,695,397,000	-\$246,812,000	+\$320,096,000	+\$73,284,000
2001	\$2,510,184,000	-\$401,181,000	+\$297,503,000	-\$103,678,000
2002	\$2,088,882,000	-\$732,290,000	+\$230,190,000	-\$502,100,000

- Any policyholder has to be concerned because if an insurance company becomes insolvent, they will obviously not be there in the future when claims occur that are on a long “tail” basis. (This means that the claims occur many years after the policy was written.)
- Also, prepaid premium dollars are typically not returned to insureds. For example, if an insured pays a \$100,000 premium for an annual policy and the carrier becomes insolvent after six months, the unearned remaining six month premium would not be returned.
- Cheaper is not always better.

Gotcha #7

I bought a policy because of the lowest premium. I told the agent, “Give me what I have now.” It did not pay off in a claim because the agent did not assess what I really needed as compared to what I had in my previous policies.

- Your agent is an “order taker” unless you insist on more. Do not count on an inept agent to even get the order right.

GENERAL GOTCHA'S

- Use an agent that is also an insurance counselor and establish a collaborative special relationship with that person. Let that person assess your needs and bring options to you that will protect your assets from loss.
- Look at the entire picture in this order:
 - The agent's expertise and qualifications. (*We mean the person who will actually be doing the work, not a dressed up front person.*)
 - The carrier's financial strength (*The A.M. Best rating.*)
 - The carrier's claims paying reputation (*This is often a well kept secret. Your agent may know but wants to get your business, and the carrier with the bad claims paying reputation may have the lowest price.*)
 - The policy terms and conditions (*And what endorsements are available to modify these terms and conditions.*)
 - The premium

Gotcha #8

I failed to list all of my entities as named insureds on all of my policies. I thought it was automatic.

- Policies do not automatically pick up related names.
- There is no forgiveness for not getting it right.
- Do an inventory of all of your past and present entities.
- Verify with state authorities that each of the current entities is a valid entity.
- Make a policy grid and mark an "X" where an entity is listed.

	Entity Name	Property	Liability	Auto	WC	Umbrella	EPL	D&O	Fiduciary	Crime
1.	ABC Corp.	X	X	X	X	X	X	X	X	X
2.	XYZ Corp.	X	X	X	X	X	X	X	X	X
3.	Jones Partnership	X	X	X	X	X	X	X	X	X

GENERAL GOTCHA'S

- If the entities listed are not consistent, ask for endorsements adding the missing names.
 - If the entity is not listed, it is not covered automatically (except for a limited number of days for some new entities) even if it is a subsidiary of a stated entity.
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Gotcha #9

The adjuster denied my loss because I had a driver with a recent drunk driving offense. I did not include this driver on my list of drivers because it would have resulted in a higher premium.

- You violated the concealment, misrepresentation or fraud clause.
- A claim can be denied as a result of concealment, misrepresentation or fraud.
- The following is the standard policy language:

A. CONCEALMENT, MISREPRESENTATION OR FRAUD

This Coverage Part is void in any case of fraud by you as it relates to this Coverage Part at any time. It is also void if you or any other insured, at any time, intentionally conceal or misrepresent a material fact concerning:

1. *This Coverage Part;*
2. *The Covered Property;*
3. *Your interest in the Covered Property; or*
4. *A claim under this Coverage Part.*

- Note that it applies before and after a claim. It applies “at any time.”
 - Note that it applies to all insureds in a multiple named insured policy. If any one named insured is involved in the misrepresentation, all insureds will be affected.
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Gotcha #10

I do not have a great deal of patience with the purchasing of insurance or management of risk. I have never even had a claim.

- This can result in multiple claim problems.
 - The following language should be removed from an insurance buyer's vocabulary:
 - “Just quote what I have now. Email it to me, and I will make my decision.”
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GENERAL GOTCHA'S

- “I’ve never had a loss. Insurance to me is a waste of money.”
- “I’m sorry, but I cannot accept your quote because I have a lower quote from someone else.”
- “I really don’t have time to meet with you, so just renew it the same way it was.”
- “If someone stole from me, I would surely know about it.”
- “I have a certificate of insurance from the subcontractor.”
- “The landlord buys the insurance on the building.”
- “Here are the specifications I have prepared. Just quote these items so I can compare everyone’s quote.”
- “I have paid insurance premiums for all of these years. Now that I have turned in one claim, the insurance company has denied the claim. They are all a bunch of crooks!”
- “Damage to my product being transported is taken care of by the common or contract carriers that I use. I don’t need separate transit coverage.”
- “My neighbor was covered for this loss.”
- “My friend pays less.”
- “We bid the insurance every year as a matter of corporate policy.”
- “We have five agents quoting this renewal.”
- “They can only take my liability limits, so I don’t want an umbrella policy.”
- “Let’s leave Harry off the list of drivers. The drunk driving ticket he received was his first ticket, and I don’t think he’ll ever do that again.”
- “I never take the loss damage waiver coverage when I rent a car. My personal insurance covers it.”
- “When I rent a car, I rent it in the company name, so I don’t have any liability for accidents or even damage to the car.”
- “When I rent a car in my personal name, the company policy will cover any claims arising out of that rental.”

GENERAL GOTCHA'S

- “If I list one name on the policy, it will pick up any other related name.”
 - “I have 100% coinsurance on my policy, meaning that the insurance company will have to pay 100% of the loss.”
 - “Twelve months is plenty of time to rebuild my building.”
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PROPERTY INSURANCE GOTCHA'S

Gotcha #1

My claim was denied because the insurance company said that the Statement of Values I signed had unrealistically low values. The insurance company denied my claim based on misrepresentation.

- Property insurance applications will often require a Statement of Values, especially when blanketing together multiple buildings into one limit or when applying an agreed value clause that waives coinsurance penalties.
 - Be diligent regarding the representation of values. Even when the limits are blanketed a reasonable basis of how the values were determined is required or the blanket limit or the entire claim could be disallowed based on fraud or misrepresentation.
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Gotcha #2

I violated the “coinsurance” standards, and my claim was reduced. I don’t even understand what that means.

- Coinsurance on buildings, personal property or equipment requires that you insure no less than the percentage indicated on the declarations page of your policy (such as 80%, 90% or 100%) of the actual property values that exist at your location. If you fail to do this, you are penalized in proportion to the deficiency.
- Example:

Building limit actually insured:	\$1,000,000
After the loss an appraisal says the building replacement cost is:	\$2,000,000
Roof blew off and claim is:	\$500,000
You promised to insure 100% of the building replacement cost values.	
You will only collect:	\$250,000

PROPERTY INSURANCE GOTCHA'S

- Coinsurance is ambiguous. Is the standard your cost, or is it the cost of a general contractor that is a union contractor, or is it the cost of a non-union contractor, etc.? These all produce different replacement costs. The policy does not set forth the standard you should use. What you should have insured, which is the basis of the penalty, is actually established by the insurance carriers after the fact.
- Reach agreement in advance about the values you are using.
- Always secure an endorsement or check the box on the property insurance policy called “Agreed Value,” or buy the policy without a coinsurance clause (which costs more).
- The insurance company will require you to sign a Statement of Values affirming that you believe the values you are using are correct.
- Be able to provide support for the basis of the values you use.
- Have appraisals that support your values if possible.
- Sign the form with the statement that it is to the “best of your knowledge and belief.”
- When you value inventory, be sure to value finished goods on a selling price basis (with most insurance carriers).
- In determining values, be sure to include property of others, such as leased property or customer owned property. (Also be sure that customer owned personal property is marked on the policy declarations as being covered.)
- Do not disregard values because they “cannot burn” (i.e. concrete forms). These are includable in insurance values and the coinsurance computation, and failure to include all values can result in severe penalties after a loss occurs.
- Include leasehold improvements in personal property values.
- A 100% coinsurance clause is not better than 80% or 90%. It is worse because a 100% coinsurance clause is more stringent.

Gotcha #3

I lease a building that I own to a tenant, and the lease requires that the tenant buy the insurance on my building. The building was destroyed, and I have been unable to collect from my tenant's insurance carrier.

- You allowed someone else to control the insurance on your asset. This is a big mistake.
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PROPERTY INSURANCE GOTCHA'S

- Never let a tenant buy insurance on a building that you own. It is seldom done correctly.
- The tenant could have the cheapest and most inadequate policy covering your asset.
- The tenant's acts could negate your coverage (e.g. arson or failure to maintain sprinkler or alarm systems).
- You may not be listed as an additional insured for property insurance in which event there will be no coverage because the tenant's policy covers only its insurable interest, not yours.

Gotcha #4

I had a fire, and the insurance company wants to deduct physical depreciation from the settlement.

Buildings:

- Failed to ask for “replacement cost” coverage on property insurance policies can create a major reduction in a loss settlement.
- The policy starts with “actual cash value” coverage but does not define what this means.
- Generally, “actual cash value” is determined based on actual replacement of the building or personal property less physical depreciation but not always.
- Example: A 20-year-old roof blows off, and it is determined that the roof has a 20-year life. The result is no recovery under an “actual cash value” policy.
- If the coverage is replacement cost, you will receive a new roof if you actually repair or replace the roof.
- Be certain that the declarations page indicates “replacement cost.”

Personal Property:

- Same concept as buildings except here even if you have replacement cost coverage, you may only receive the value of a used item. This is because the insurance company can pay the cost to repair or replace with other property of “comparable material and quality used for the same purpose,” meaning used.
- Even if you have the replacement cost endorsement, it does not apply to “stock” unless you ask for this and it is indicated on the declarations page of the policy.

PROPERTY INSURANCE GOTCHA'S

- You must include the value of outdoor property even if it is not susceptible to damage. Even if the outdoor property, for example, is concrete forms that cannot be destroyed, the value must be included or you will be in violation of coinsurance or misrepresentation clauses.
 - If you are responsible for the replacement of personal property owned by others, such as leased equipment, include the replacement value in your value determination, but be sure that personal property of others is marked or endorsed as being included on the policy declaration page.
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Gotcha #5

I had replacement cost coverage on my building, yet the insurance company only paid the actual cash value (replacement cost less physical depreciation).

- The standard policy requires that in order to get replacement cost, you must notify the insurance company of your intent to actually replace the property within 180 days of the loss or damage.
 - After notifying the insurance company of your intent to replace the property, you must do so “as soon as reasonably possible after the loss or damage.”
 - The difference between “actual cash value” and “replacement cost” is not paid until you actually replace or repair the property.
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Gotcha #6

My adjuster reduced my business interruption claim saying that my business interruption limit did not comply with the policy requirements.

- You must insure business interruption to the standard indicated on the policy (i.e. 80%, 90%, or 100%) for loss of income.
- Here is how it works. In order to collect fully on business interruption subject to a coinsurance clause, the policy indicates that you must do as follows:

We will not pay the full amount of any Business Income loss if the Limit of insurance for Business Income is less than:

- a. The Coinsurance percentage shown for Business Income in the Declarations; times*
- b. The sum of:
 - (1) The Net Income (Net Profit or Loss before income taxes), and*
 - (2) Operating expenses, including payroll expenses,**

That would have been earned or incurred (had no loss occurred) by your “operations” at the described premises for the 12 months following the inception, or last previous anniversary date, of this policy (whichever is later).

PROPERTY INSURANCE GOTCHA'S

- Example: (12 months after inception of the policy)

Net income: \$500,000
Operating expenses: \$5,000,000 (including payroll)
Total: \$5,500,000

Had a \$1,000,000 limit on the policy.

Should have had a \$5,500,000 limit on the policy.

Had a \$750,000 loss.

Will collect $\$750,000 \times 18.2\% = \$136,500$.

- You must look ahead 12 months in determining values.
- Solution: Have an agreed amount endorsement which requires that you provide a worksheet to the insurance company. This will waive the application of coinsurance and would result in payment of the full claim.
- The policy does not require any specific form and does not require a signature, but you must have both an agreed value endorsement and file a worksheet.

Gotcha #7

The adjuster only paid my business interruption claim during the period it took to rebuild my building, but I lost a major customer. It will take me a long time to get that business back.

- The policy pays during the period of time it should take to repair or replace what was damaged plus, in most cases, 30 days.
- The problem is that you have just lost your biggest customer and your reduction in sales and resultant income will go on for years.
- Solution: Extend the 30 days to one year or more. Some carriers will provide “unlimited.” This is called the “extended period of indemnity.”
- Do not confuse what you have to insure as established by a business interruption worksheet and what you should insure based on how long your reduction in sales and income will be. Twelve months is seldom going to be an adequate recovery period for any business.

Gotcha #8

I was underinsured on one building, but the adjuster would not pay the full amount of my loss even though I was overinsured on another building.

PROPERTY INSURANCE GOTCHA'S

- You failed to blanket building and personal property when you had multiple locations.

- Example:

	<u>Limit on Policy</u>
Building #1:	\$1,000,000
Building #2:	\$750,000
Building #3:	\$800,000
Building #4:	<u>\$250,000</u>
Total:	\$2,800,000

- A fire occurs and destroys building #1. The actual replacement cost turned out to be \$1,300,000.
- The result under specific limits is a recovery of \$1,000,000.
- With blanket limits, the recovery is \$1,300,000 (assuming no coinsurance clause and no fraud in the establishment of values).
- Always insist on blanket limits with multiple buildings.

Gotcha #9

I had one building, and I had a total loss. It turns out that I was underinsured on the building damage but overinsured on personal property. What did I do wrong?

- You failed to blanket the building and personal property limits together when you had one building (or even with multiple buildings).
- Example:

	<u>Limit on Policy</u>
Building #1:	\$1,000,000
Personal Property:	<u>\$500,000</u>
Total:	\$1,500,000

- If a loss of \$1,300,000 occurs to your building structure, you would collect \$1,000,000 under separate limits. You would collect \$1,300,000 under a blanket limit.

Gotcha #10

I have leased buildings. When the policy was written, they were all occupied, but I had a vacancy several months later and was only 29% occupied. The pipes burst in the winter because of freezing, and the adjuster denied my loss of \$400,000 saying there was no coverage at all.

PROPERTY INSURANCE GOTCHA'S

- You violated the vacancy clause.
- If a building is “vacant” at the time of a loss, there will be no coverage at all for:
 - Vandalism
 - Sprinkler leakage from automatic fire sprinkler systems
 - Glass breakage
 - Water damage (e.g. bursting of pipes)
 - Theft (e.g. building wiring or air conditioning equipment)
 - Attempted theft

All other losses, such as a fire, are reduced by 15%.

- A building is “vacant” if:
 - Owner of the building is the insured: At least 31% of the square footage is not rented and used by a lessee to conduct customary operations and/or used by the building owner to conduct customary operations.
 - Tenant is the insured: It is “vacant” when the portion rented does not contain enough business personal property to conduct customary operations.
- Solution to the vacancy clause: Secure a vacancy permit endorsement or purchase a policy that does not have a vacancy clause (assuming you have disclosed the fact that the building or suite is vacant because failure to do so would be a misrepresentation).

Gotcha #11

I had a bursting of water pipes in my fully occupied building. The adjuster said that I was not covered.

- You did not have the correct Cause of Loss forms. You failed to purchase the Broad or Special Cause of Loss form. Instead, you purchased the Basic Cause of Loss form which does not include water damage.
- Almost all property insurance policies have what is referred to as “Cause of Loss” forms.
- Three general forms apply: the Basic form, the Broad form, and the Special form. Only purchase the Special form unless the insurance company will not offer this and you have no other options (such as with a vacant building).
- The Basic form covers only the following perils and none other:

PROPERTY INSURANCE GOTCHA'S

- Fire
 - Lightning
 - Explosion
 - Windstorm or hail
 - Smoke
 - Aircraft or vehicles
 - Riot or civil commotion
 - Vandalism
 - Sprinkler leakage
 - Sinkhole collapse
 - Volcanic action
- Under the Broad Cause of Loss form, the exact same perils apply as in the Basic form except the following perils are added:
- Falling objects
 - Weight of snow, ice or sleet
 - Water damage (but not flood from the outside)
- The Special Cause of Loss form eliminates the naming of perils and instead indicates that it will cover all risks of physical loss except for what is excluded. Property insurance claims that are not covered under the Special Cause of Loss form:
- Ordinance or law changes*
 - Earth movement*
 - Governmental action
 - Nuclear hazard
 - Utility services damage*
 - War and military action
 - Flood*
 - Mudslide or mud flow
 - Backup of sewers, drains or sumps*
 - Water under the ground surface pressing on or flowing or seeping through foundations, walls, etc.
 - Power surge*
 - Electrical arcing*
 - Smoke from industrial operations*
 - Wear and tear
 - Rust
 - Fungus*
 - Deterioration
 - Nesting or infestation, discharge or release of waste products or secretions by insects, birds, rodents or other animals

PROPERTY INSURANCE GOTCHA'S

- Mechanical breakdown*
- Dampness or dryness of atmosphere
- Changes in or extremes of temperature
- Marring or scratching
- Explosions of steam boilers*
- Seepage of water for more than 30 days
- Water caused by freezing unless you maintain heat or drain the equipment
- Dishonest or criminal acts
- Pollution except as a result of specified losses
- Neglect to use reasonable means to save and preserve property after a loss
- Interior damage by rain, snow, sleet, ice, sand or dust unless the building or structure first sustains damage by a covered cause of loss
- Collapse (See separate insurance "Gotcha #12")

* Can typically buy endorsements to delete or modify these exclusions.

- The advantage of the Special Cause of Loss form is that it covers more perils and the burden is on the insurance company to prove that an exclusion applies.

Gotcha #12

My roof collapsed, and the adjuster denied the loss saying it was a design defect.

- The Special or broadest Cause of Loss form excludes losses as a result of the collapse of a building with certain exceptions.
- The collapse must be caused by:
 - A specified cause of loss as defined as fire; lightning; explosion; windstorm or hail; smoke; aircraft or vehicles; riot or civil commotion; vandalism; leakage from fire extinguishing equipment; sinkhole collapse; volcanic action; falling objects; weight of snow, ice or sleet; water damage.
 - Decay that is hidden from view.
 - Insect or vermin damage that is hidden from view if not known to an insured.
 - Weight of people or personal property on the roof.
 - Weight of rain that collects on a roof.
 - Use of defective material or methods in construction, remodeling or renovation but only if the collapse occurs during the course of the construction, remodeling or renovation.

PROPERTY INSURANCE GOTCHA'S

- If the collapse occurs after construction, remodeling or renovation is complete, coverage will apply if the collapse is as a result of the specified causes of loss of decay, insect or vermin damage, weight of people or personal property, or weight of rain collecting on a roof.
 - Furthermore, if a roof collapses as a result of earthquake and there is no earthquake coverage, no coverage would apply.
 - Design error is not covered.
 - Some insurance carriers do not have this type of exclusion or modify it so that a design error in the roof would not exclude collapse arising out of excessive snow. Look for a modification of the concurrent loss exclusion.
-

Gotcha #13

A product I manufacture was at a subcontractor's location, and the building was destroyed arising out of a lightning strike. The subcontractor's insurance company adjuster denied the loss for my property saying that the subcontractor was not negligent. My insurance company only paid \$10,000.

- Off premises property is not covered on your policy at a subcontractor's location in excess of \$10,000.
 - If in transit, there is no coverage unless you have added transit coverage.
 - A subcontractor is typically responsible for damage to your property only if it was negligent absent an agreement that expands that responsibility.
-

Gotcha #14

The adjuster said that the mold I found after my bursting of water pipes is not covered.

- Mold remediation is not covered under most property policies.
 - This is the case even if there is a covered loss first, such as a bursting of water pipes.
 - Try to negotiate at least a sublimit for mold remediation arising out of a covered loss.
 - Mold remediation can be expensive, and it is difficult to secure adequate limits.
-

PROPERTY INSURANCE GOTCHA'S

Gotcha #15

The adjuster denied my fire loss because the sprinkler system did not function properly.

- Protective safeguards, such as sprinkler or alarms systems, need to be maintained in good working order if a “protective safeguard” endorsement has been added by the insurance company.
 - This clause allows the insurance carrier to deny a fire or burglary loss if the sprinkler system or alarm system you said you had in place was not maintained in “complete working order,” whatever that means.
 - Avoid this clause at all costs even if you have to pay a higher premium to obtain a policy without it.
-

Gotcha #16

I had a total loss. My insurance company paid for the building replacement and debris removal but not for the cleanup and remediation of the land caused by the fire. My uninsured expense was \$200,000.

- Environmental cleanup of land after a fire is limited to only \$10,000 under the basic policy.
 - The cost of cleaning up land at your location as a result of a fire can be substantially higher than \$10,000 after the Michigan Department of Environmental Quality does its inspection.
 - Negotiate higher limits.
-

Gotcha #17

After an inspection and before any loss, the insurance company said that I had to insure my building for \$85 per square foot, and I did so. After a loss, the insurance company refused to pay the actual replacement cost of \$135 per square foot. I did what they told me to do, and now they won't pay the difference.

- Relying on building values estimated by the insurance company is at your own peril.
 - Insurance carriers often use average values in determining the minimum building values that you should insure.
 - Do not rely on these values to determine what you actually should insure. Their minimum values are typically not realistic and are low.
-

PROPERTY INSURANCE GOTCHA'S

- There is often a big difference between what the insurance company says you have to insure and what you should insure.
 - A letter from an underwriter indicating what you had to insure does not alter the policy which speaks for itself. Only the four corners of the policy count.
-

Gotcha #18

I insured my building based on the insurance company's estimate of replacement cost, but it was not enough because it failed to contemplate debris removal expense.

- Include the estimated cost of debris removal in calculating the limit to be insured on a building.
 - The standard policy provides a sublimit, not an additional limit, of 25% of the loss for debris removal expense, but if this amount when added to the loss amount exceeds the limit, the standard form adds only \$10,000.
 - You have the option to add more, and some carriers automatically add more.
 - Be liberal on the high side in establishing values.
-

Gotcha #19

My insurance company recommended that I use their building insurance values. I thought I could rebuild for less and insisted on using my own building values in order to lower my premiums. I had a blanket limit and did not think that I could get hurt. I had a fire and now they are disregarding the blanket limit based on misrepresentation.

- Always use values recommended by the insurance company if they are higher than your estimate of values.
-

Gotcha #20

I had a big fire. The water used to extinguish the fire and the fire itself damaged my underground pipes and foundations. The adjuster refused to pay for this portion of the loss.

- Underground pipes and foundations are excluded under the standard policy.
 - Always add this coverage. Underground pipes and foundations can be damaged in the event of a major fire.
-

PROPERTY INSURANCE GOTCHA'S

Gotcha #21

The policy declaration page for property insurance did not state that personal property of others in my possession was included, and the adjuster will not pay for this property that was damaged in a fire.

- The standard form requires this. Even if you have included personal property of others in your values, other than leased personal property (that is covered under the owned business personal property definition), you must insist that “included” be indicated under the property declarations page for personal property of others.

Gotcha #22

My insurance company will not pay for upgrades in reconstruction costs required by building code changes. Where did I go wrong?

You need to add an ordinance or law endorsement to your policy. This covers:

- The increased cost of reconstruction because of building code changes.
- The demolition cost of portions of the building required by building code changes or the demolition of the undamaged portion of the building because it can no longer be used as a result of the loss of grandfathering under building codes.
- The value of the undamaged portion of the building that must be torn down because of a loss of grandfathering.
- Without this coverage, the insurance company only owes the value of the building before the loss, not as it has to be rebuilt because of building code changes.

Gotcha #23

It took longer than I thought to rebuild my building because of delays in getting a building permit, and the adjuster will not pay for delays in rebuilding my building because of building code issues.

- Business interruption only covers the time it should take with due diligence to repair or replace the building. The problem is you may not be able to obtain a building permit because of zoning or building code requirements. If you are delayed for six months because of this, for example, you will not be covered under standard business interruption insurance.
 - This coverage can be purchased by an endorsement to your business interruption coverage.
-

PROPERTY INSURANCE GOTCHA'S

Gotcha #24

I had a big fire, and the insurance company denied the loss based on an exclusion I never was aware of. I sued the insurance company and my agent, and ultimately I won. However, the legal fees were close to the settlement I received, and now I find out that I cannot recover my legal fees.

- This is correct. The worst that can happen to an insurance company is that they will have to pay the loss plus, in limited circumstances, some interest.
 - You typically cannot recover your legal fees.
-

Gotcha #25

I inflated a property insurance claim in one small area in order to get a “kickback” from the contractor. The adjuster denied the entire loss.

- Misrepresenting any portion of a property claim can void the entire claim.
-

Gotcha #26

I had a major fire that destroyed my building. It took me 16 months to get back into business by the time I settled with the insurance company, obtained bids and had the building rebuilt. The claims adjuster indicated that my insurance company will only pay 12 months of my business income loss. My agent had sold me business interruption coverage on an actual loss sustained basis. There was no specific limit.

- The mistake here was to purchase “actual loss sustained” coverage because it limits the recovery to 12 consecutive months of business interruption loss.
 - It is better to secure business interruption coverage with a specific dollar limit but no specific time limit for rebuilding, assuming you proceed with due diligence. Of course, be sure that the specific limit is high enough.
 - You should then extend this time period by at least an additional 365 days to cover business losses after construction is completed.
 - When you determine your limit, contemplate at least 24 months of business income loss or maybe more.
-

PROPERTY INSURANCE GOTCHA'S

Gotcha #27

I had business interruption coverage. The power recently failed, shutting down my business for several days. My agent indicated that I do not have any coverage for loss of income because of power failure.

- Standard business interruption coverage does not cover loss of utilities unless you buy a specific endorsement covering this type of loss.
-

Gotcha #28

I had a fire to my retail store. As a result, several thousand dollars of money that was located in my safe was destroyed. The insurance company has denied coverage for the loss of money because of this fire.

- The standard property insurance policy does not cover accounts, bills, currency, food stamps, money, notes or securities.
 - The solution to this problem is to buy money and securities coverage which covers damage to or theft of money.
-

Gotcha #29

As a result of a fire, I had significant damage to my lawns and landscaping at my business. The damages were caused by not only the fire, but by the water and the fire trucks. The adjuster indicated that the damage to outdoor property such as this caused by fire is limited to \$1,000 but not more than \$250 for any one tree, shrub or plant.

- This is correct.
 - The solution is to add coverage for landscaping.
-

Gotcha #30

A vehicle recently damaged my electric gate system at my plant. The insurance company has denied this loss.

- This is a correct denial. The standard insurance policy limits coverage for damage to outdoor fences to only fire, lightning, explosion, riot or aircraft. Vehicle damage is not covered.
 - There is an extension that can be purchased to provide this coverage on a broader basis.
-

PROPERTY INSURANCE GOTCHA'S

Gotcha #31

I recently had a major business interruption loss. In order to establish what my losses were, I had to pay a CPA a great deal of money. I submitted the bills for the CPA to the insurance company as a part of this loss, and the costs were denied.

- This is a correct denial. Costs associated with proving your loss are not covered under the standard form.
 - Some insurance companies will provide coverage on a broader policy but only where they require that you incur the expense.
-

Gotcha #32

As a result of a business interruption loss caused by a fire, I had to lay off my employees. I wanted to pay for them under my business interruption coverage while the building was being rebuilt. However, the adjuster indicated that ordinary payroll had been excluded from my policy.

- Many business interruptions policies will exclude by an endorsement “ordinary” payroll. This means that the insurance company will only cover payroll of officers, executives, department managers, and employees under contract.
 - Ordinary payroll limitations can be modified to include as a covered payroll expense other important employees that do not come under the normal ordinary payroll exceptions.
 - Be very careful with ordinary payroll limitations. You may be required to layoff (and therefore lose on a long-term basis) many important employees not included within the normal ordinary payroll exceptions.
-

Gotcha #33

I have not had any damage to my building; however, my business has been interrupted because my key customer had a fire. The adjuster indicated that I do not have any business interruption coverage for this.

- This is a correct denial. Business interruption covers only covered causes of loss at your scheduled locations.
 - However, you can purchase coverage by an endorsement to your policy for dependent properties listing locations of your key customers or suppliers.
-

PROPERTY INSURANCE GOTCHA'S

Gotcha #34

I have a manufacturing plant, and I have customer molds and dies in my possession. One of those molds was stolen, and the insurance company has agreed to cover only \$2,500 for this theft. The replacement value is \$50,000.

- This is correct. The standard insurance policy only covers \$2,500 for theft of molds or dies actually owned by you.
 - An endorsement can be secured to provide coverage for this, and many insurance companies have broader policies that do not have this limitation.
 - Do not forget to add “personal property of others” to the policy declarations page.
-

Gotcha #35

I use common carriers or contract carriers in my business. A major loss occurred to a trailer that was transporting my products. The common carrier indicated that they are not liable for the loss because the damage was caused by lighting that struck the trailer.

- This is correct. Common and contract carriers are only liable for their negligence, and even then only up to limited amounts based upon the terms and conditions of a bill of lading.
 - Never rely on the insurance provided by a contract or common carrier. You should have your own coverage that pays regardless of negligence.
-

Gotcha #36

My phone system box is attached to an outside wall. As a result of seepage through that wall during a heavy rainstorm, the phone box was damaged and has to be replaced. The insurance company will not pay the claim.

- This is a correct denial. Under the standard insurance form, there is no coverage for seepage through walls causing building or personal property losses.
-

Gotcha #37

I own a major transformer that is located at the back of my property. As a result of a power surge, the transformer was destroyed and has to be replaced. The cost of the replacement is \$60,000. The adjuster says that I am not covered because I did not have equipment breakdown coverage.

PROPERTY INSURANCE GOTCHA'S

- This is a correct denial. Property insurance policies exclude damage as a result of steam boiler explosion even if the building is destroyed; damage as a result of mechanical breakdown; and damage as a result of electrical arcing or power surges.
 - This coverage can be purchased under what is generally referred to as a boiler and machinery policy or an equipment breakdown policy and should be a standard part of every insurance program.
-

Gotcha #38

I am a just-in-time supplier. As a result of a fire, we were unable to supply our product, and an assembly line of our customer was shut down. The insurance company has indicated that it will not pay under business interruption the \$720,000 that was charged by my customer for shutting down its assembly line for 24 hours.

- This is correct. Business interruption insurance does not cover contract penalties of this nature.
 - Some insurance carriers will provide contract penalties coverage by endorsement.
-

LIABILITY INSURANCE GOTCHA'S

Gotcha #1

I was sued because of a slip-and-fall in my parking lot, and I lost. I had \$1,000,000 in liability insurance and thought it was enough. Now I have lost my business.

- Your primary liability exposures are:
 - Premises injuries
 - Products causing injuries
 - Auto accident injuries
 - Each of these exposures to loss can result in a catastrophic injury or damage involving multi-millions of dollars in losses. Do not assume that you can only be sued up to the insurance limits you carry. The successful plaintiff's attorney will take everything you own if your liability limits are not sufficient.
-

LIABILITY INSURANCE GOTCHA'S

Gotcha #2

I was sued, and the adjuster denied my claim because one of the liability coverage exclusions applies.

- The commercial general liability exclusions in the typical standard policy are as follows.
- Contractual or assumed liability
 - Liability assumed from others by way of a contract indemnification clause is not covered except for bodily injury or property damage liability for certain contracts.
 - Even when the contract is covered, claims arising out of injuries prior to the agreement are not covered. Often agreements require the assumption of prior unknown injuries.
 - Indemnification of claims for invasion of privacy, false arrest and other similar injuries are not covered under the limited contractual liability coverage.
 - Breach of contract is not covered.
- Liquor related claims
 - Even if you are not in the business of selling, serving or distributing liquor, coverage may not apply if you make a charge for the company picnic.
- Autos, aircraft or watercraft
 - If any insured uses or owns a private plane or watercraft and causes injury, there is no coverage.
 - There is an exception for non-owned watercraft less than 26 feet. (Business owners could own watercraft that could be used in business or use non-owned watercraft that are 26 feet or larger.)
 - Automobiles, whether owned or non-owned, are excluded under commercial general liability forms. (You need to add non-owned auto coverage by endorsement to the commercial general liability policy or secure an auto policy in order to cover the automobile exposure.)
- Products recall expense
 - No coverage is provided even if it is necessary in order to prevent an injury claim.
- Pollution

LIABILITY INSURANCE GOTCHA'S

- “Pollutants” mean any solid, liquid, gaseous or thermal irritant or contaminant, including smoke, vapor, soot, fumes, acids, alkalis, chemicals and waste. Waste includes materials to be recycled, reconditioned or reclaimed.
- Exceptions to pollution exclusions:
 1. Smoke from a hostile fire
 2. Fumes from heating equipment to heat the building
 3. Bodily injury or property damage arising out of heat, smoke or fumes from a hostile fire
 4. Pollution from your products

(Many carriers do not even provide these limited exceptions.)

- No liability coverage is provided for injury arising out of:
 1. Accidental spills
 2. Fumes from hi-los
 3. Injury from Legionnaire’s disease
 4. Injury from mold
 5. Injury from sewer backup
 6. Illegal dumping of your waste without your knowledge
 7. Fumes from a room being painted
 8. Anything else except for the limited exceptions indicated above

(Most insureds need a special environmental policy to cover cleanup or injury arising out of an environmental spill or other event.)

■ Damage to buildings you lease from others

- Coverage for damage to buildings you lease from others is limited to \$100,000 and only for fire damage. Water damage or other perils are not covered.
- A 50,000 square foot leased building typically has a replacement cost of \$5,000,000.
- You can buy broader coverage and higher limits by way of a tenant’s legal liability endorsement which covers your negligence that causes damage to a building you lease from others.
- Review lease clauses carefully, particularly the “maintenance or repair clause,” which if not properly drafted will require you to repair or replace the building even if you are not negligent. (Not covered even if you purchase the tenant’s legal liability form.)
- Look for a waiver of subrogation clause. This is a desirable clause if correctly drafted because it can block a landlord’s insurance company from suing you as a tenant that damaged or destroyed the landlord’s building. Be careful, however, because most waivers of

LIABILITY INSURANCE GOTCHA'S

subrogation do not apply if the landlord cannot collect under its policy. We suggest that this clause look like the following:

Waiver of Subrogation. *Notwithstanding anything to the contrary contained in this Lease, Tenant and Landlord, respectively, release each other from any and all liability or responsibility and waive any rights of recovery, whether direct or by way of subrogation or otherwise, against each other, their agents, officers and employees, for any loss of or damage to their respective property, which occurs in or about the Building or Premises whether or not covered by any insurance, regardless of the cause of origin or even if such loss or damage shall have been caused by the fault or negligence of the other party or anyone for whom such party may be responsible. In addition, each party hereby waives the subrogation rights of its insurers against such other party. Landlord and Tenant each agree to obtain such a waiver in all applicable insurance policies.*

Gotcha #3

I failed to list a location on the liability policy. Someone was injured, and the adjuster said that I was not covered.

- The liability policy must list the address of any location you own, lease or occupy as of the inception date of the coverage each year. Locations added after the inception date are typically covered without reporting it until the policy expiration date.
-

LIABILITY INSURANCE GOTCHA'S

Gotcha #4

I had an “umbrella” policy and thought that it was a catch-all for all claims not covered by my other policies.

- Umbrella excess liability will not solve all of your problems. Assume that it only provides higher liability limits for your premises, products and auto claims. A few policies will be broader than the primary premises, products and auto policies. However, do not count on this.
 - It is not really an “umbrella.”
 - It is really not even “excess.” In many cases, the umbrella is not even as broad as the primary insurance. For example, the primary liability policy may have the three basic pollution coverage exceptions and the umbrella policy may not have these exceptions.
-

LIABILITY INSURANCE GOTCHA'S

Gotcha #5

I forgot to send a COBRA letter, and the employee sued me for health benefits that would have been covered.

- Employee benefit mistakes are not covered unless you have purchased employee benefit legal liability coverage as an endorsement to your commercial liability policy or unless you purchase a fiduciary liability policy.
 - Poor administration of employee benefits, such as technically incorrect COBRA letters or failure to send a COBRA letter when required, can lead to major losses.
 - Do not do COBRA letters yourself. Use an outside professional source.
-

Gotcha #6

I had a certificate of insurance from a subcontractor. When I went after the subcontractor because of a claim, I learned that I was not actually an additional insured on its policy.

- Relying on certificates from subcontractors making you an additional insured is a big mistake.
 - Certificates do not modify insurance policies.
 - Certificates alone are not enough. You need an indemnity agreement and verification that you actually have been added as an additional insured to the subcontractor's policy.
-

Gotcha #7

I just received a big audit on my liability insurance policy that included intercompany sales. Can they do that?

- Yes. Avoid this by endorsing the policy to exclude intercompany sales.
 - The downside is that intercompany lawsuits which are ordinarily covered now will be excluded unless you negotiate otherwise.
 - Intercompany lawsuits, which are liability claims brought by one named insured against another named insured, are covered automatically unless excluded by an endorsement. Avoid these endorsements.
-

LIABILITY INSURANCE GOTCHA'S

Gotcha #8

A customer fell in my parking lot and was injured. The customer indicated that she was not going to make a claim and that the medical bills would be taken care of by her health insurance. Now she has filed a lawsuit against me and my insurance company has denied the loss because I failed to report it at the time.

- The liability insurance policy has specific language indicating: “You must see to it that we are notified as soon as practicable of an occurrence or an offense which may result in a claim.”
- In this case, the insured knew about the occurrence but did not report it, prejudicing the insurance company’s right to investigate and to prepare for a claim.
- Also in this case, the insured actually knew about the occurrence. However, in other cases, an employee may know about it and may not report it to an officer so that the policy conditions can be complied with. This may constitute imputed knowledge of the employer. In this type of situation, an endorsement known as the Broad Form Notice of Occurrence endorsement can be added to the policy. This endorsement basically indicates that if an officer did not know about it, the insurance company cannot deny the loss for late reporting even though an employee knew about it.
- This endorsement is not part of the standard policy.

Gotcha #9

I manufacture products that go to Mexico. My product caused an injury in Mexico and I was sued in Mexico. My insurance company denied the loss indicating that my commercial general liability policy does not cover lawsuits in Mexico.

- This is correct. The commercial general liability policy only covers injuries occurring within the United States, Puerto Rico and Canada.
- There is an extension covering all parts of the world if the injury arises out of goods or products made or sold in the United States, for example, but only if the lawsuit itself is brought on the merits in the United States.
- The answer here is to purchase an international policy to cover lawsuits that may be brought in other countries arising out of your products.

Gotcha #10

A customer fell in my parking lot. Because the injuries were minor, I did not want to report

LIABILITY INSURANCE GOTCHA'S

the claim in order to avoid a premium increase, and I settled the claim myself but failed to obtain a proper release. The injured person has now sued me, and the insurance company denied the loss.

- The policy indicates the following: “No insured will, except at that insured’s own cost, voluntarily make a payment, assume any obligation, or incur any expense, other than first aid without our consent.”
-

Gotcha #11

We chartered a large party boat for customer entertainment. A customer was injured on the boat and sued us. Our insurance company denied the claim.

- This is a correct denial. Commercial liability policies exclude bodily injury arising out of the use of any watercraft rented or loaned to any insured. The only exception to the exclusion is non-owned watercraft less than 26 feet long.
 - An umbrella policy may provide coverage for larger watercraft, or the primary policy can be endorsed to increase the size of the watercraft that is covered.
-

Gotcha #12

My customer wants me to incur the expense of recalling products that we manufacture because it has a defect which could cause injury. My insurance company has denied the cost of doing this even though it could save them millions of dollars in potential claims.

- The standard occurrence based commercial liability policy covers only bodily injury, property damage and certain mental injury type perils, such as invasion of privacy, that actually occur during the policy period. There is no coverage for products recall expense even if it could prevent a loss.
-

Gotcha #13

I did not purchase high liability limits because I have a corporation and felt that I was isolated from liability. As a result of an injury occurring at my building, I was sued personally. I thought that I was isolated from liability because of my corporate status.

- Individuals are always liable for their own negligence. For example, if an individual is employed by that person’s own corporation or LLC, that person can be sued for their individual negligence. A physician that has a medical practice owned by a professional corporation can still be sued personally for individual acts of malpractice.
-

LIABILITY INSURANCE GOTCHA'S

- If you perform any services within a building, you could be personally liable for negligent acts that result in injury.
-

Gotcha #14

I had a child care business 20 years ago. A child was injured while I had this business, and now 20 years later I have received a claim by that child. My policies have been destroyed. My agent does not have a copy, and the insurance company cannot find a record of my having any insurance.

- Liability insurance policies should never be destroyed. This is because the burden is on the insured to prove that coverage existed. In the case of minors, minors can make a claim within one year of reaching maturity at age 18.
-

Gotcha #15

I own a health club, and we always require children of members and their parents to sign releases before using the health club. A claim was made by a minor, and the court indicated that the release was not valid.

- This is correct. In Michigan, the release of a minor by the minor or by the minor's parents has no validity.
-

Gotcha #16

I am a contractor. I was sued because someone was injured arising out of my job, and the insurance company denied the loss indicating that I had a professional liability exclusion.

- Professional liability exclusions are often applied to commercial liability policies by insurance companies for insureds in many types of professions, including general contracting.
 - The original intention of this type of exclusion was to exclude economic damages arising out of improper advice or providing improper professional services.
 - The way these exclusions are written, however, is that they apply to bodily injury or property damage arising out of professional services. These exclusions should be unacceptable.
-

Gotcha #17

My customer was sued because of my operations and my products. My customer indicates

LIABILITY INSURANCE GOTCHA'S

that our agreement required that I add the customer as additional insured to my liability insurance. I thought this was automatic; however, the adjuster has denied the defense of this claim because I did not actually add this customer as an additional insured to my policy.

- This is a correct denial. The standard liability policy does not automatically add customers as an additional insured.
- You need to have an endorsement that automatically adds customers and other parties where a written contract requires you to add them as additional insured.
- You must, however, be certain that the additional insured language will include claims arising out of your products inasmuch as insurance carriers typically limit coverage under these circumstances to “your work” and not your products.

WORKERS' COMPENSATION GOTCHA'S

Gotcha #1

I was fined by the State of Michigan and sued by an employee because I failed to buy workers' compensation insurance.

- Workers' compensation insurance is required by law if one full-time employee or three part-time employees in Michigan.
- Failure to comply can result in:
 - \$1,000 fine per day.
 - Imprisonment for not less than 30 days or more than 6 months for each day of failure to comply.
 - An action in tort for negligence with few defenses and without the benefit of the limited benefits that Workers' Compensation Act provides.
- If you are a sole employee of an LLC you own, you must have workers' compensation.
- You can exclude owners, but this creates a coverage gap with health insurance which assumes that workers' compensation is in place. Do not do it.

WORKERS' COMPENSATION GOTCHA'S

Gotcha #2

I changed insurance carriers last year because the premiums were a lot lower. After the policy expired, the insurance company did a workers' compensation payroll audit, and the classifications were changed by the auditor. The insurance company wants me to pay a big additional premium.

- A change of classification in an audit after the policy expires can cost an insured thousands of dollars. Most insurance carriers audit workers' compensation payroll by classification after the policy expires each year.
 - Reach an agreement up front regarding classifications.
-

Gotcha #3

I had an employee living in another state who was injured in an auto accident and made a workers' compensation claim that has been denied.

- If an employed sales rep, for example, works from home in another state, there is no coverage for an injury to the employee, such as an auto accident on the job, unless that state is listed on the workers' compensation policy.
 - Failure to obtain workers' compensation can result in civil and criminal sanctions.
 - Just because you pay from Michigan does not change the place of employment.
-

Gotcha #4

I was audited after a policy expired and was charged an additional premium because a subcontractor did not have liability or workers' compensation coverage.

- This can cause major additional premium charges on liability and workers' compensation policies after the fact.
 - You must obtain certificates from each and every subcontractor you use indicating that the subcontractor has workers' compensation and liability coverage.
 - If the subcontractor is a sole proprietor without any employees and is not an employee that you say is a subcontractor, you can avoid audit charges. However, you need to have documentation to establish this.
-

WORKERS' COMPENSATION GOTCHA'S

Gotcha #5

We paid a big bonus last year to an executive, and now the insurance company is charging a big additional premium.

- Failure to understand payroll caps for executive officers or members of an LLC can result in a big additional premium.
 - The payroll of highly compensated executive officers of corporations or members/managers of LLCs can be capped to approximately \$80,000 (depending on the insurance carrier) in Michigan. This can make a big difference in premiums and does not affect the benefits that can be collected.
 - Be careful with LLCs in other states. The rules may be different.
-

Gotcha #6

I employed a 17-year-old high school student without working papers. The 17-year-old was injured, and the insurance company doubled the claim and then asked me to pay half of the amount.

- This is correct. In Michigan, the insurance company must pay a double claim in the event you hire or employ a minor illegally, and that means without working papers or doing jobs that were not permitted under the law for minors. The insurance company has the right to demand that you pay the penalty amount which is one-half of the claim.
-

CRIME GOTCHA'S

Gotcha #1

I did not buy crime insurance, thinking that my property insurance policy automatically provided coverage.

Major crime exposures:

- Employee dishonesty of insured's property.
 - Employee dishonesty of client property.
 - Forgery by other than employees.
-

CRIME GOTCHA'S

- Funds transfer coverage.
- Theft or holdup by outsiders.

These are not covered by standard property policies.

Gotcha #2

I had a big employee embezzlement claim, and it was denied even though I had employee dishonesty coverage because of a small prior theft by the employee.

- Employee dishonesty is cancelled automatically as to any “employee” immediately upon discovery by the insured of any “theft” or any other dishonest act committed by the employee whether before or after becoming employed by the insured.
-

Gotcha #3

My embezzlement claim was denied because I did not turn it in on time.

After you discover a loss or situation that may result in a loss, you must:

- Notify the insurance company
 - Notify law enforcement
 - Provide a “proof of loss” within 120 days.
-

Gotcha #4

My partner stole a great deal of money.

- No coverage for acts committed by your partners or members of an LLC under standard employee dishonesty.
 - Some insurance carriers will reduce the loss for members of an LLC based on a percentage of ownership. Others will deny coverage even if the employee was a 1% owner of an LLC.
-

Gotcha #5

I had an embezzlement claim and discovered that I had insufficient limits.

CRIME GOTCHA'S

A 2009 study by Marquet International Ltd. (www.marquetinternational.com) shows:

- The average employee dishonesty loss is over \$1,000,000.
 - The top two industries were financial services and manufacturing.
 - The average scheme lasts 4.5 years.
-

Gotcha #6

I just discovered that an employee stole \$250,000 from me five years ago, but I only had \$10,000 in coverage at that time. Now I have \$1,000,000 in coverage, but the adjuster said that I am only covered for \$10,000 because I had the “loss sustained” form.

- You failed to purchase employee dishonesty on a “discovery” basis and instead purchased “loss sustained” coverage.
 - The difference between the two forms is that under the “discovery” form you will have coverage for prior year losses and the limit that will apply will be the current year’s limit, not the lower limit that you had in past years.
 - Annual limits do not “stack” under employee dishonesty coverage.
-

Gotcha #7

It cost me \$50,000 in CPA expense to prove a \$100,000 theft by an employee. I had \$100,000 in coverage, and the adjuster indicates that I can only collect \$100,000, not my \$150,000 total loss.

- Investigative expenses to prove employee dishonesty are not covered.
 - You need to prove your loss, and this requires a forensic CPA in most situations.
 - Can add this with many carriers.
 - \$25,000 should be the minimum limit.
 - Even if the loss is covered, the expense cost is within the limit and not outside the limit.
-

Gotcha #8

Checks were stolen from our office, and the thief forged the checks. We thought that the bank would assume any losses arising out of the forgery. The bank failed to do so citing the

CRIME GOTCHA'S

provisions of the Uniform Commercial Code that apply in this type of situation. The insurance company indicated that I did not have forgery coverage.

- This is correct. The Uniform Commercial Code has several provisions that apply.
 - Furthermore, the bank-customer contract also has provisions that limit the bank's responsibility.
 - This type of agreement indicates that the customer is responsible for monitoring and reviewing the activity on its account as well as looking for improper and unauthorized signatures, alterations, forged endorsements and other irregularities.
 - The customer has 30 days from the time of the bank's mailing of the statement to notify the bank of any discrepancies.
 - The Uniform Commercial Code authorizes the bank to afford the customer a reasonable amount of time not exceeding 30 days to examine its statements of account and notify the bank.
-

AUTO GOTCHA'S

Gotcha #1

I had \$300,000 in auto liability coverage. My employee killed one person and injured three more. The claimants have sued for millions of dollars in damages.

- You obviously had insufficient auto liability limits.
 - Example: Macomb County judgment involving an auto accident where one person did not die in the amount of \$57,700,000 (10/28/05 *Hattan v C.A. Hull Co.*).
 - Buy as much auto liability insurance as you can afford.
-

Gotcha #2

We placed the owner's personal car on our company business auto policy. An accident occurred and the claim was denied as to the owner because he failed to lease the car to the business.

- An employee owned or leased car added to the company auto policy is not covered as to the employee (likely the business owner) without adding the "employee as lessor" endorsement and having a lease agreement; adding "broad form drive-other-car" coverage; and listing the employee and children of driving age as drivers.
-

AUTO GOTCHA'S

Gotcha #3

We rented a car on business. The car was stolen, and the rental company put \$35,000 on my credit card. My auto insurer will only pay \$25,000 for the car repair and will not pay loss of profits.

- You failed to secure adequate coverage for damage to rental cars by:
 - Relying on your business or personal insurance for complete coverage (loss of profits, diminution of values, repair cost, disparity of opinion as to damages are not covered) is a big mistake.
 - Relying on the rental car company “loss damage waiver” (where purchased) is a mistake.
 - Consider American Express Premium Car Rental Program - \$24.95 per rental period.
 - However, be sure that your business auto policy has rental car physical damage coverage as well as non-owned and hired car liability insurance for injury claims.
-

Gotcha #4

An executive had an at-fault accident while using a personal car on company time. Our company as well as the executive was sued. The executive had a \$300,000 limit, and the executive's insurance company paid the \$300,000. However, the claim was \$2,000,000. Our business insurance paid \$1,700,000 under “non-owned autos.” Now our insurance company has sued the executive to recover the \$1,700,000 it paid.

- Failure to add “employee as additional insured” coverage for employees using personal cars on company time is a mistake. The premium is small, and it may be available at no cost.
 - This adds the insured's commercial auto limits and umbrella to the employee's personal auto limit.
 - This also blocks your insurance company from suing your own employee to recover what it has to pay because of the employee's negligence.
-

Gotcha #5

I told the insurance company that some of my business vehicles were garaged in a location with lower rates, and this was not true. A claim has been denied.

- This is a misrepresentation and can void coverage.
-

AUTO GOTCHA'S

Gotcha #6

We had a big auto injury claim arising out of a driver that we did not disclose because we knew about a drunk driving offense. The claim was denied.

- If you had a principal driver with a drunk driving offense or an otherwise bad driving record or you had youthful operators that were not disclosed on a list of drivers given to the insurance carrier, you do so at your own peril.
 - If a major claim occurs, coverage could be denied because of fraud or misrepresentation.
-

Gotcha #7

I had a new leased car that was totaled in an accident. The leasing company wants to have the entire lease paid off. The insurance company indicates that it only owes the actual cash value of the car at the time of loss, and there is a big difference.

- This is correct. The insurance company only owes you the actual cash value, which is about the same as market value, of the car. The leasing company may want a much higher amount.
 - You need a lease gap clause in the lease agreement or lease gap insurance with your insurance company.
-

MANAGEMENT PRACTICES GOTCHA'S

Gotcha #1

Our directors were sued by the bank claiming an improper financial statement.

- Private companies need directors and officers liability coverage just like public companies.
-

Gotcha #2

Our company was sued by a competitor for "tortious interference" in its business. Our liability policy did not cover this.

- Always add "entity" coverage to your D&O policy.
 - Breach of contract claims are not covered, nor are copyright infringement claims.
-

MANAGEMENT PRACTICES GOTCHA'S

- This may, however, provide legal defense costs and more if an insured is sued by a customer or competitor.
-

Gotcha #3

We were sued because a supervisor was sexually harassing an employee. Coverage was denied under our general liability policy.

- This claim is excluded by the commercial general liability policy.
 - You need Employment Practices Liability coverage for claims that can be made against you by your employees for:
 - Discrimination
 - Wrongful discharge
 - Sexual harassment
-

Gotcha #4

My outside salesperson has been accused of sexually harassing an employee of one of our customers. This claim was denied under our commercial general liability policy and under our Employment Practices policy.

- You failed to purchase “third party coverage” when purchasing Employment Practices coverage.
 - This covers an insured’s employee who harasses a customer’s employee.
-

Gotcha #5

I was the decision maker on our 401(k) plan and health benefits program. I have now been sued personally for not providing an adequate array of investment options. Am I covered under our company general liability policy?

- No. You failed to purchase Fiduciary Liability coverage to cover the entity and personal liability of the “fiduciaries” for actions or non-actions relating to ERISA plans (401(k) plus health).
-

Gotcha #6

An employee claims that we should have paid overtime, and we are now being audited by the U.S. Department of Labor for failing to comply with the law regarding overtime

MANAGEMENT PRACTICES GOTCHA'S

payments. Our legal fees are significant. Is this covered under general liability insurance?

- No. You need wage and hour defense coverage under your Employment Practices Liability policy.
-

Gotcha #7

I have a policy covering Employment Practices Liability. I received a lawsuit from a former employee for wrongful discharge. The insurance company has denied the loss indicating that I did not report the claim when I received a document from the EEOC.

- This is correct. Under the Employment Practices Liability policy, the receipt of an EEOC form constitutes a claim and must be reported. Under the claims made policy, failure to report a claim as soon as practicable or within the policy period allows the insurance company to deny the loss.
 - There is a big difference between “claims made” and “occurrence” based policies.
 - Claims made policies use the date that the claim was made as a trigger date for coverage.
 - Occurrence based policies use the date of the event.
 - Employment Practices Liability coverage is on a claims made basis. The claim itself must be promptly reported or coverage can be denied.
-

BUILDER'S RISK GOTCHA'S

Gotcha #1

We had a fire in our new building that was mostly completed and only 1% occupied. The adjuster denied the loss citing the occupancy exclusion on the builder's risk policy.

- Partially occupying without permission of the insurance company may void coverage.
-

Gotcha #2

Because of that same fire, we lost a job that was planned for this new building. As a result, we lost a large amount of profits.

- You failed to buy business interruption coverage under the builder's risk policy.
 - This coverage is needed for delays in occupancy caused by a fire or other perils.
-

BUILDER'S RISK GOTCHA'S

Gotcha #3

We had a builder's risk policy covering our building while it was under construction. We determined the value that was insured based upon the building contract amount. After construction began, we made a number of changes increasing the cost by 25%. We did not change the limits on the builder's risk policy. We had a major loss to the building costing \$1,000,000 to repair. The insurance company only paid \$750,000. The adjuster said that we did not insure 100% of the completed value.

- This is correct and similar to coinsurance. You must always insure at least 100% of the completed value of the building or you are penalized in proportion to the deficiency.
-

PERSONAL INSURANCE GOTCHA'S

Gotcha #1

I had a homeowners policy but did not personally occupy the home. I rented it to someone else several months ago. Subsequently, the home was destroyed by fire. The insurance company has denied the loss.

- The home must be occupied as your personal residence if you have a homeowners policy.
 - This means that vacant homes or homes that are rented to others are not covered for property damage or liability claims under the homeowners policy form.
 - Rental homes should be written on "dwelling," not homeowners policies.
 - Vacant homes should be written on special policies designed for vacant homes.
-

Gotcha #2

I had a water backup in my home's lower level which did substantial damage, and the adjuster said that I only had \$5,000 in coverage.

- Typically \$5,000 is all that is covered under most homeowners policies for this type of claim.
 - Drywall, carpeting and furniture damage to lower levels arising out of water backup or sump pump overflow can often exceed \$75,000.
 - Use a carrier that allows higher limits.
-

PERSONAL INSURANCE GOTCHA'S

Gotcha #3

As a result of a water loss in my home, I had a great deal of mold growth that had to be remediated. The adjuster said that I only had \$5,000 in coverage.

- Again, this is a typical limit.
- Look for an insurance company that offers higher limits.
- Understand that even with higher limits, mold remediation coverage is only provided if there is a covered water event first.
- Bad ventilation or leaky roofs that cause water damage are not covered causes of loss, and there is no coverage for damage or mold arising out of this.
- Even if you have mold coverage, you must be diligent in extracting water after a water event.

Gotcha #4

I have a home based business. A package delivery person fell in my driveway while delivering a business package and sued me. The insurance company denied the claim based on the business exclusion.

- The personal liability section of your homeowners policy excludes any business related claims. Add a home office business endorsement to your homeowners policy or add this location to your business policy.

Gotcha #5

We had heavy rains that seeped through my basement walls causing a great deal of damage. The insurance company denied the loss.

- No coverage is provided for a true exterior flood that enters your home from the outside.
- No coverage is provided for any type of seepage under most policies.
- Add flood coverage; however, even flood coverage may not cover all losses.

Gotcha #6

The adjuster said that he was not going to pay for the theft of my jewelry.

PERSONAL INSURANCE GOTCHA'S

- The typical homeowners policy limits theft or disappearance of jewelry to \$1,000-\$2,500 unless specifically scheduled.
 - The advantage of scheduling is that you avoid the policy deductible and sublimits for theft of jewelry. The coverage is broader (e.g. disappearance is covered), and the policy will pay off the scheduled amount in the event of a total loss (if stated value coverage is added).
-

Gotcha #7

My friend was using my snowmobile and hit a tree, sustaining major injuries. I have now been sued, and my homeowners carrier denied the loss under the personal liability section of that policy.

The typical homeowners policy does not automatically cover:

- Four wheelers
- Jet skis
- Snowmobiles
- Dirt bikes
- Small electrical ride on toys
- Watercraft (other than small boats)

You need to secure specialty policies with high liability limits for these exposures.

Gotcha #8

My aunt was able to obtain an auto discount because I placed my name on the title of her auto. An adjuster for a person injured by her in an accident says that I am responsible for injuries arising out of the use of this vehicle. She did not have enough insurance and failed to add my name as an additional insured.

- Under Michigan law, the titleholder of a vehicle is liable for whatever injuries occur with the vehicle.
 - Do not expose yourself to this potentially catastrophic exposure by unnecessarily adding your name to the title of a car when you do not control the insurance.
 - If you have already done so, verify that the vehicle is insured and that your name is listed as an insured and that liability limits are at least \$1,000,000 or preferably higher.
-

PERSONAL INSURANCE GOTCHA'S

Gotcha #9

I had a fire that destroyed a dwelling that I rent to others. The dwelling was not occupied at the time of the fire because I was between tenants. The insurance company has denied the claim.

- This is a correct denial for many insurance companies that write dwelling policies. It allows for vacancy for only 30 days, and after that there is no coverage whatsoever.
- The solution is to purchase a policy with a vacancy permit, although it should be noted that the perils covered on this type of policy could be limited. For example, there may not be coverage for vandalism or water damage.

Gotcha #10

I had a fire at my home, and the limit I had on my homeowners policy was not sufficient to replace my home. My agent had sold me guaranteed replacement cost coverage which she said at the time would increase the limit automatically if it was not sufficient at the time of a major loss. The insurance company indicated that I violated that clause by not reporting any improvements to my home of \$5,000 or more at the start of those improvements.

- This is correct. Even with guaranteed replacement cost coverage, if you do not report improvements that could increase the replacement cost of your home by more than \$5,000 (or whatever rules an individual carrier sets forth in the endorsement), the clause does not apply and the limit that you purchased is the most you would receive.
- For the purpose of establishing limits on a homeowners policy, you can use the insurance company's replacement cost estimate as a guide; however, these estimates may not be realistic and may not reflect the actual replacement cost of your home.
- Although the guaranteed replacement cost provision is good to have, purchase a dwelling limit that will properly protect you without that clause.
- Never confuse market value and replacement cost.

Gotcha #11

My home was destroyed by fire. The named insured on the policy was myself and my husband. The insurance company denied the loss indicating that the home was actually owned by a marital trust that we had formed and deeded the house to. The marital trust was not listed on the insurance policy as an insured.

PERSONAL INSURANCE GOTCHA'S

- This is correct. You must name the actual owner of the home on the policy in order to be properly insured.
-

Gotcha #12

I lease my home and had a renter's policy covering my contents and my personal liability for bodily injury or property damage claims. I had a major water loss arising out of my child stuffing paper towels down the toilet. The landlord's insurance company is asking me to pay over \$100,000 to reimburse it for what it paid to repair this home. My insurance company said that I am not covered for this claim.

- This is a correct denial. A renter's policy with most insurance companies covers only fire, smoke or explosion damage to the dwelling or apartment you rent from others.
 - Some insurance carriers will add coverage for water damage.
-