DISASTERS HAPPEN PRE-PLANNING AND LEASE PROVISIONS ARE A NECESSITY

Clients frequently call for advice when a fire or other casualty event has damaged the community. While casualty events can vary significantly, we do see a number of recurring issues associated with them. This month we discuss the key issues that commonly arise when a casualty event occurs at a community. We will refer to "a fire", but it could be a flood, mold infestation, asbestos situation, etc.

Most fire-related issues involve insurance. Some landlords still only "strongly recommend" renter's insurance. However, the clear industry best practice is to require tenants to purchase renter's insurance, or have some forced damage liability program in place. For example, some landlords require tenants to pay a fee for each month the tenant fails to carry renter's insurance. The landlord then uses the fees to self-insure, by establishing a damage claim pool or reserve. We always advise our clients to require renter's insurance or maintain an equivalent. Renter's insurance may not (usually does not) cover everything, but some renter's insurance is better than none.

Surprise! Believe it or not, the THS situation board is littered with situations involving renter's insurance surprises. One surprise is that the tenant's insurance doesn't cover damage caused by the fire. Insurance coverage varies widely. If you are going to require insurance and you should, you should know what is covered and what is not.

Typically, most renter's insurance only covers liability, and does not cover property damage. Usually this means that if a tenant starts a fire in 301, and 301, 302, and 303 are damaged, the insurance company is only going to pay for the damage to 302 and 303. For another example, if ninety percent of the casualty events, over the last five years, involved tenant water incidents, your renter's insurance better cover water-related events.

A second surprise is that there is no coverage at all for any of the fire damage. The tenant who started the fire was supposed to have insurance but doesn't. The tenant never purchased the insurance or failed to maintain the insurance. You should never be surprised that a tenant doesn't have required renter's insurance. If you require insurance, never allow a tenant to move in without proof of purchasing insurance. Your lease should also give you the right to purchase insurance for the tenant, and charge the insurance cost to the tenant as additional rent. Regardless of your policies, no policy requiring renter's insurance will succeed without monitoring. However, we frequently hear from clients that they "don't have time or the resources to monitor" tenant insurance. Fortunately, you don't have to. Many insurance related multifamily vendors offer both insurance and insurance monitoring. With the cost being paid by the tenants and the work being done by the insurance vendor, a landlord has no excuse for not monitoring tenant compliance with insurance requirements.

When a fire occurs, you should promptly investigate and inspect, notify insurance, determine obligations, and communicate the community's position to the tenants. Regardless of any other investigation, to protect the community's interests, you should always conduct your

own investigation, and complete a detailed incident report. Tenants, like all people, are more likely to give an accurate account of an incident nearer the time of the event. When given time to think about an event, tenants may change their story to avoid financial responsibility.

The fire department and insurance investigators may have different motivations. For example, tenant insurance companies have gotten much more aggressive about pursuing subrogation claims. The insurance company will pay out under the tenant's renter's insurance, but then tries to recover the money paid out by asserting someone else was at fault for the fire. The community is usually the "somebody" that the tenant's insurance company tries to recover from. An incident report where the tenant admits fault should prevent the tenant's insurance company from asserting the community was somehow at fault, and otherwise defeat their attempt to get their money back from you.

Insurance companies also want to pay the least amount as possible. Accordingly, an insurance company may not thoroughly inspect adjoining units for damage. Your onsite team should always conduct a detailed inspection of any potentially damaged areas as soon as possible. Fire is almost always considered an emergency and frequently requires immediate repairs or other actions. However, before a third-party vendor takes any action at your property, you should always confirm their qualifications, and their action plan. Fires at asbestos-containing properties are particularly problematic. Accordingly, you should discuss containment of the asbestos with the vendor, and confirm that no action on the part of the vendor will result in spreading any asbestos. If a fire exposes asbestos but also resulted in water damage, you don't want the vendor blowing asbestos all over the place by using blowers to dry the carpet. For those of you wondering, yes, this really has happened.

Any insurance policy requires that the insurance company be notified when a damage event occurs. Most communities do a good job providing notice to applicable tenant renter's insurance companies. However, many times, communities fail to notify their own insurance company of a potential claim. A community fails to notify their carrier because the community concludes their own insurance won't be used. Most communities have very high deductibles and frequently, the damage is less than the deductible. High deductibles combined with the assumption that the tenant's renter's insurance will pay leads to the erroneous conclusion that the community's insurance carrier shouldn't be notified.

However, failing to notify the community's insurance carrier can be a serious mistake for several reasons. If you don't provide notice of a claim by a certain date, all insurance policies bar you from making a claim in the future. For example, if notice is not provided on what is believed to be a $15,000 claim, you might be out of luck if a year and half later it turns out to be a $150,000 claim. Providing notice to your own carrier protects you if the damage turns out to be far worse than anyone anticipated. Additionally, insurance companies make two promises in every insurance policy. The insurance company promises to pay (duty to indemnify) and promises to defend you against claims (duty to defend). Most folks forget about the insurance company's duty to defend. In many instances, you can avoid paying significant legal fees by notifying your insurance company and demanding that they defend you (hire and pay the attorneys to deal with litigation or legal demands arising from a fire).

Many problems for a community arising from a fire are caused by inadequate lease language. Absent contractual language, the law determines rights and obligations between a tenant and a landlord. Unless the premises are totally destroyed, Colorado law is not specific or particularly helpful in sorting out the rights and obligations between a landlord and a tenant after a fire. At common law, absent a lease provision, the tenant remains liable for the rent even if the property burned to the ground. Similarly, at common law, the landlord has no duty to repair or rebuild upon partial damage or destruction. Even absent a lease provision today, the landlord can terminate a lease under Colorado law upon destruction of the premises. However, unless the tenant was at fault (caused the fire), no Colorado court is going to hold the tenant liable for damages or the remaining rent if the premises are destroyed due to no fault of the tenant.

Because most fires don't result in the destruction of the premises, inadequate lease language frequently comes into play. Any partial damage scenario will quickly test the sufficiency of your lease. Leases often fail the partial damage scenarios, fire damage can turn into a legal quagmire, and a logistical nightmare (constant arguments with tenants which impede repairs and result in bad PR for the community).

Specific lease language addressing partial damage scenarios solves this problem. Every lease should have a clause giving the landlord the right to terminate upon partial destruction. Based on the tens of thousands of situations we have been involved with, we rate this clause in the top 10 most important lease clauses. If you do not have a casualty clause, contact our office to learn more about adding this important clause to your lease.

The Colorado Warranty of Habitability Act (WHA) also demonstrates the importance of lease language. Specifically, WHA states that it does not prevent a landlord from terminating a rental agreement as a result of a casualty or catastrophe to the dwelling unit without further liability to the landlord or tenant. If your lease gives you the right to terminate after a fire, the WHA makes it clear that you can do this, and thus you can terminate the tenant's lease and defeat any WHA claims raised by tenants because of the fire. What is not clear is if the WHA gives you the right to terminate based upon a casualty event absent lease language. Arguably it does, but of course you are in a stronger position with termination language.

Your lease should also address the alternative living accommodations issue. If one or more of the buildings at your community burns to the ground, both the tenants and the press will expect you to arrange for and pay for the displaced tenants to live somewhere else (alternative living accommodations). This problem should be addressed in the lease as well. Specifically, the landlord may arrange for alternative living accommodations, but is not obligated to provide the tenant with alternative living accommodations if the unit is destroyed. Further, landlord strongly recommends that the tenant obtain renter's insurance that provides alternative living accommodation coverage. It's one thing to tell the tenants and Channel 9 you're not responsible. However, the community looks much better if you can say that you told the tenant up front about this potential issue, and encouraged them to take action to avoid the very situation they are in now.

When it comes to fires, or any casualty for that matter, the key is to have a plan. Renter's insurance is a huge part of any plan. You can't just assume that the insurance your tenants sign

up for will cover all damage scenarios. You should verify that the insurance would yield the expected result. If your tenant renter's insurance program won't cover what you want and need, find a program that will. Keep in mind that a community's insurance program is a lot easier to control and monitor than renter's insurance from outside providers, e.g. State Farm, Farmer's, Allstate, etc. For business reasons, you may allow outside insurance. However, there is no legal requirement that you allow residents to have outside insurance. Once you have the insurance equation solved, make sure that your lease doesn't leave you in no man's land. Your lease should clearly define your rights in the event of a fire or other casualty, including specifically setting forth the procedures to be followed. While we are always here for you, your lease should be so clear you don't need to call us.