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Beware Of Insurance Coverage On Vacant Buildings



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I write about commercial real estate negotiations, deals and legal issues.



A vacant building may create insurance headaches. GETTY IMAGES

When a property owner moves its business out of a building or loses a major tenant, the building may sit vacant for an extended time. Aside from enduring the pain of lost revenue and having to pay real estate taxes and

other expenses to carry a building that doesn't produce revenue, the owner also needs to think about a possible pitfall in its insurance coverage.

When an insurance company issues a typical property insurance policy, the company looks at the insured building and assesses the risks of that building. If the building is actively occupied and someone conducts business there, the risks of vandalism and "malicious mischief" against that building are relatively low. But if nothing is going on in the building, then it's an invitation for vandalism and "malicious mischief."

In response, property insurance policies typically say that if a building is vacant or unoccupied for a certain period – typically 30 or 60 days – then the policy won't cover certain losses, such as damage done to the building by vandalism and "malicious mischief."

This so-called vacancy exclusion has spawned plenty of litigation. For example, sometimes there's a difference between "vacant" and "unoccupied." The policy might exclude only one of those circumstances. In that case, courts might need to figure out what the two words mean and how they differ. If very limited activities are happening in the building, it might be "vacant" but not "unoccupied," or vice versa.

And what does "malicious mischief" mean? If someone deliberately sets a fire next door and it burns down this building, is that "malicious mischief," which might not be covered if this building is vacant or unoccupied? Or, in the alternative, is it a "fire," which the policy might still cover even for a vacant or unoccupied building?

See Next Page

These are fascinating questions, which one can try to answer by reading probably hundreds of court cases.

A careful owner will, of course, have no interest in any such undertaking, or paying lawyers to do it. Instead, a careful owner will know that as soon as a property becomes vacant or unoccupied, or both, the owner should take a hard look at the building's property insurance policy. Does it have a vacancy exclusion? And exactly what does that vacancy exclusion say?

If the building will stay vacant or unoccupied, the owner should consider whether it makes sense to notify the insurance carrier. That notice will probably lead to a repricing of the insurance coverage. It might even lead to a change in coverage or cancellation.

It's better for the owner to know about that problem before the owner needs to file a claim rather than after. If the owner does nothing and then makes a claim because of a loss to which the vacancy exclusion applies, the owner faces the risk that the carrier will deny coverage. In that case, the owner will

have paid insurance premiums for nothing except the right to sue the insurance company and probably lose.

Bottom line: As soon as a building becomes vacant, beware of the vanishing insurance policy, at least as the vacancy exclusion relates to vandalism, “malicious mischief,” and sometimes other perils.



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I help buyers, sellers, borrowers, lenders, tenants, property owners, and other commercial real estate market participants identify and achieve their business goals. To do that, I need to understand risk, security, numbers, value, financeability, flexibility, and exit strategy. Some legal issues matter a lot and many don't. It's important to know the difference. I write extensively on commercial real estate law and practice – over 300 articles and five books on leasing, lending, and other areas, with some emphasis on ground leases. I occasionally serve as an arbitrator or expert witness in complex real estate disputes. That lets me see how transactions go wrong. Often, the problems could have been avoided by keeping it simple and following the money, but everyone got sidetracked. As a Forbes contributor, I try to tell stories that teach worthwhile lessons for real estate deals. **Read Less**

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