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Professional Liability: Managing the Hidden Exposures Facing Today's Real Estate Professionals

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FROM A CLIENT'S PERSPECTIVE

**Paul S. Rutter, Esq. Executive Vice President
Thomas Properties Group**

The management of a public real estate company relies on the management liability coverages (D&O, E&O, and Employment Practices) to protect the company in a wide range of activities, including:

- **Construction and Development Services**
- **Asset and Property Management Services**



FROM A CLIENT'S PERSPECTIVE

- **Investment Advisory Services**
- **Brokerage Services**
- **Real estate consulting services**
- **Securities claims**
- **Duties as a partner in ventures with investors**
- **Dealing with employees in the current environment**



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FROM A CLIENT'S PERSPECTIVE

Real Estate Services

Companies that provide third parties with real estate services, including property management and brokerage, entitlement and development services, real estate consulting, and investment advisory services face exposure to claims of malfeasance or failure to perform services with the appropriate standard of care.



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FROM A CLIENT'S PERSPECTIVE

Real Estate Services

In this environment, the potential for claims is even greater, with underperforming assets, broken deals and failed investments in every part of the country.

- **While third party services can generate substantial revenues to a real estate company, they also can be the source of potential exposure to a company from claims by third parties arising out of these services.**



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FROM A CLIENT'S PERSPECTIVE

Real Estate Services

- **A property manager may be exposed to claims by the property owner and by the owner's tenants who can make claims against both the owner and the property manager for alleged failures to properly manage and protect the property and its occupants. These claims can include alleged failure by the property manager to comply with contracts affecting the property, such as reciprocal easement agreements or CCRs.**



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FROM A CLIENT'S PERSPECTIVE

Real Estate Services

- **Companies need to be aware of the standard of care in the industry and evolving expectations for the level of services to be provided in similar properties, especially in the area of security and access control.**



FROM A CLIENT'S PERSPECTIVE

Real Estate Services

- **Development services agreements for entitlement and construction management work can provide significant fees and income to the developer but bring with them potential for large claims in light of the large risks and expenditures being managed by the developer. What are appropriate E&O limits and what is demanded by the client?**



FROM A CLIENT'S PERSPECTIVE

Partnership Relationships

Relationships with partners provide another source of potential claims for a company to consider:

- **As a managing or general partner, you need to balance the demands and goals of investors and partners with those of the public shareholders.**



FROM A CLIENT'S PERSPECTIVE

Partnership Relationships

- **As a managing or general partner, you need to balance the demands and goals of investors and partners with those of the public shareholders.**
- **The company must be confident that the management liability coverage protects the company and its officers and directors from claims that might arise from its role as a general partner**



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FROM A CLIENT'S PERSPECTIVE

Lender Relationships

Relationships with lenders create another area of concern regarding potential claims.

Real estate loans usually contain representations and warranties as well as financial and other covenants in favor of the lender.



FROM A CLIENT'S PERSPECTIVE

Lender Relationships

- **These financial covenants are often direct obligations of a parent company even if made at a subsidiary level on a property specific loan.**
- **Most non-recourse loans have carve outs from the non-recourse provisions for "bad acts" by the borrower or its general partner.**



FROM A CLIENT'S PERSPECTIVE

Lender Relationships

- **As the real estate market has deteriorated, many covenants under loans across the industry have been stressed or have tripped and lenders will look closely for opportunities to recover losses through the non-recourse carve outs. This may lead to claims by investors and partners in the borrower or in the general partner that the company has mismanaged the property, or has exposed them to potential recourse liability under the loan through its actions.**



FROM AN INSURANCE BROKER'S PERSPECTIVE

**William Holden, Managing Director
Wells Fargo Insurance Services**

Issues from Broker's Perspective

Brokers always represent the client and must help the client consider how to identify and achieve long and short term goals through use of Risk Management Tools.



FROM AN INSURANCE BROKER'S PERSPECTIVE

Management Liability Coverages:

- **Directors & Officers Liability** for liabilities arising from the management of the business
- **Professional Liability** for the day-to-day operational liabilities
- **CyberLiability** for liabilities arising from website, privacy invasion and technology protection



FROM AN INSURANCE BROKER'S PERSPECTIVE

- **Employment Practices Liability for:**
 - First Party EPL claims brought by employees
 - Third Party EPL claims for sexual harassment or discrimination brought by non-employees

- **Crime Insurance, including Computer Theft and Fraudulent Funds Transfer**



FROM AN INSURANCE BROKER'S PERSPECTIVE

Prepare the Client's risk for review by underwriter

1. Corporate Governance Review to analyze in depth practices and procedures

- Accounting
- Banking
- Legal
- Employee Governance
- Investor Relations
- Board Management
- Loss Control Procedures



FROM AN INSURANCE BROKER'S PERSPECTIVE

2. Prepare an Underwriter Presentation

- **Executive Summary - brief but detailed description of client's business**
- **Strengths of the Company and Management**
- **Financial Highlights and Analyses**
- **Areas of Concern - The Risk Factors to eliminate or mitigate their effects**
- **Recent Developments - What Has Been Happening with the Client's Business**



FROM AN INSURANCE BROKER'S PERSPECTIVE

- 3. Communications with underwriters: What the client wants and needs**
- **Coverages desired**
 - **Limits of Liability for each line**
 - **Retentions**
 - **Additional Coverages**
 - **Due dates for the quotes**



FROM AN INSURANCE BROKER'S PERSPECTIVE

Review, Negotiate and Develop Programs

- **Get Wording of policies and endorsements correct**
- **Best Time to resolve a claim is before it occurs by getting clarity in policy wording**

Bind Coverage and Deliver Correct Policies



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FROM AN INSURANCE BROKER'S PERSPECTIVE

Claims Assistance and Advocacy

- **Filing of Claims**
- **Assistance with Reservation of Rights Letters**
- **Claims Expectations in terms of coverage**
- **Assistance in coverage disputes**



FROM AN UNDERWRITER'S PERSPECTIVE

**Sabine Cain, Vice President
Chubb**

What do insurance carriers look at/look for?

Every carrier takes multiple issues in consideration when underwriting a risk but the areas of underwriting focus fall into the following categories:

- 1. The leverage of the fund itself**
- 2. Liquidity of the fund**
- 3. Overall asset quality**



FROM AN UNDERWRITER'S PERSPECTIVE

4. Management of the funds and governance

5. Appraisal methodology

Additionally the characteristics that make real estate risks most desirable are:

- Full transparency**
- Experienced, successful and stable management team**



FROM AN UNDERWRITER'S PERSPECTIVE

- **If private, a sophisticated investor base. If public, an institutional investor base**
- **Solid financial condition**
- **Clear and proven long term operating strategy**
- **Property portfolio that is well diversified and profitable**



FROM THE CLAIMS PERSPECTIVE

**Linda Pierce, Esq. Senior Vice President
Arthur J. Gallagher & Co.**

Preparing for and managing the claim process:

- **Recognizing a "Claim" and understanding reporting requirements**
- **Retention of counsel**
- **Cooperating with insurer(s)**



FROM THE CLAIMS PERSPECTIVE

- **Understanding reservations of rights**

- **Working with multiple insurers**
 - **"Other insurance" provisions**
 - **Excess carriers (*Qualcomm*)**



FROM THE CLAIMS PERSPECTIVE

- **Resolution strategy**
 - **Mediation**
 - **Arbitration**
 - **Settlement**
 - **Motion practice**
 - **Trial and beyond**