

**AMERICAN ASSOCIATION OF INSURANCE SERVICES  
INLAND MARINE GUIDE  
WAREHOUSE OPERATORS LEGAL LIABILITY  
UNDERWRITING**

**COVERED PROPERTY**

Warehouse Operators Legal Liability (WOLL) insurance is intended to provide legal liability coverage for public warehouse operators. Under this coverage the warehouse operator is the insured, and the covered property is the property of others that is being stored by the operator. The warehouse operator is responsible for the property of others under the terms of the warehouse receipt.

**Types of Warehouses**

Public warehouses are in the business of storing the property of others for a fee. This is the type of warehouse operation with which the WOLL and this Guide are concerned. There are three other commonly referred to warehouse operations:

1. Private Warehouses -- those that are owned or controlled by manufacturers, distributors, retailers, or other enterprises and are used to store their own property.
2. Bonded Warehouses -- are used to store imported property pending payment of import duties and taxes. Since the duty is due only when the property is released, an importer can withdraw the goods as they are needed, and duty fees can be stretched over a more manageable period. This type of warehouse is operated jointly by the U.S Customs authorities and a warehouse operator.
3. Contract Warehouses -- have elements of both public warehouses and private warehouses. Typically, the contract warehouse has a small number of customers with long term contracts, as opposed to a larger number with monthly agreements commonly used by a public warehouse. This type of operation usually does more handling and processing of merchandise than a public warehouse.

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## **Handling and Processing**

Although the primary function of a warehouse is to store property, it is not uncommon for the warehouse operator to offer other services. The following are some examples of these services.

1. Stockpiling -- use of the warehouse to store excess merchandise, or to keep a ready inventory of finished or component property.
2. Assembling -- use of the warehouse to put together components.
3. Product Mixing -- arranging sets of property to be shipped together at a later date.
4. Consolidation -- use of the warehouse as a central point for various shipments of merchandise. These separate shipments are then combined and shipped out together.
5. Distribution -- breaking up of one or more large shipments into smaller shipments destined for various locations.

Merchandise handling may be performed by public, contract, or private warehouses. The underwriter should obtain copies of any merchandise handling contracts or agreements.

## **Legal Liability Coverage vs. Property Insurance**

It is important to understand that the coverage afforded under the WOLL policy is not insurance for the owner of the property. The WOLL covers the legal liability of the warehouse operator for loss or damage to property of others that is stored in the warehouse. Regardless of the value of the property, the WOLL is intended to cover only that amount of a loss for which the warehouse operator is legally liable.

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## **Warehouse Receipt**

A warehouse receipt should be issued to every customer who stores property at a warehouse. The receipt:

1. gives a general description of the property stored;
2. states the monthly storage charge;
3. describes the conditions under which the property will be stored;
4. states that the warehouse operator is not liable for loss to the property unless caused by negligence (in reality warehouse operators usually must show that loss or damage was NOT caused by their negligence); and
5. provides a limitation on the amount of the operators liability for loss to their customer's property.

Typically, the limitation of an operator's liability is expressed as a multiple of the monthly storage charge. However, it can sometimes be stated as a dollar amount per pound, box, or cubic footage. The amount that the operator is legally liable for in case of loss indicates the amount of risk assumed by the underwriter.

## **Acts of God**

Damage that results from "acts of God" (e.g., lightning, earthquake) are generally considered out of the control of an operator. Warehouse operators are not usually considered legally liable for damage that results from "acts of God." However, it should not be presumed that a loss due to such occurrences will never result in the warehouse operator being found legally liable. If a warehouse operator is aware of or had been warned of an impending event (e.g., flood) but takes no action to protect the property, then the operator might be held legally liable.

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**RISK SELECTION**

To underwrite warehouse operators legal liability coverage the following information should be obtained:

1. Construction features, including:
  - a. construction of walls and roof;
  - b. height in stories;
  - c. total floor area;
  - d. total storage area;
  - e. age of building; and
  - f. age of plumbing and electrical, date of upgrade if any.
2. Occupancy, including
  - a. type of warehouse operation; and
  - b. type and extent of handling and processing.
3. Protection, including:
  - a. sprinkler system data:
    - 1) testing, and
    - 2) water flow alarm; and
  - b. premises alarm data (i.e., extent, grade, and certification).
4. Exposures including any other operations which occupy space in the building.
5. Estimated values in storage
  - a. average; and
  - b. maximum.

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6. Target Commodities (as a percentage of total):
  - a. consumer electronics;
  - b. liquor, wine, and other alcoholic beverages;
  - c. finished tobacco products; and
  - d. PC components (chips, boards, etc.).
7. Largest customers.
8. Annual storage receipts.
9. Loss history (last three years).
10. Copy of the warehouse receipt (front and back).
11. Management:
  - a. low employee turnover
  - b. formal hiring program
  - c. formal training program, including operation of machinery
  - d. safety program
  - e. claim frequency due to poor handling of property

**Financial Condition**

A copy of the warehouse operator's balance sheet and income statement should be requested and examined. Dunn & Bradstreet reports may also be ordered. A warehouse operation should be closely examined to make sure that it is financially stable. Operations which are not financially strong are especially susceptible to morale and moral hazards.

Without a strong financial base, a warehouse operation may withhold resources from security and fire protection. Underwriters need to assure themselves that equipment maintenance and procedures for commodity handling will be followed.

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## **KEY HAZARDS**

### **Fire**

Because of its catastrophic potential, fire poses the greatest threat to a warehouse operation. Construction, occupancy (operation), protection, and exposure characteristics of the warehouse location should be closely checked. Damage caused by a fire of unknown origin may be presumed to have been caused by the warehouse operator's negligence.

Protective devices such as sprinkler systems, premises alarms, and smoke and heat detectors/alarms can be highly effective loss control features. However, these protective devices are only effective if they are properly maintained and monitored. These devices should be equipped with alarms to alert the insured to low water pressure in the sprinkler system, loss of contact in the central alarm system, or malfunction of heat and smoke detectors. These protective devices and their alarms should be inspected and tested on a regular basis.

It is also important that protective devices are designed to address the exposures that are inherent in the property being stored. Stored property may include flammable and/or explosive goods as well as property that requires stacking or storage in shelves. High stacking can reduce the effectiveness of a sprinkler system and shelves can prevent water from reaching combustible goods. It should be noted that the storage of aerosol products can present an explosion and flammable projectile hazard.

Control of flammable and/or explosive property can be controlled by storing these goods in a separate fire resistive room, in a separate building or segregating them with a fire wall. The hazard created by stacking can be addressed by enforcement of clearance standards and the installation of sprinklers in shelves.

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The age and condition of wiring and heating units should be established. Old wiring may be corroded and loose, and the insulation may not meet current codes. A furnace or boiler that has been allowed to deteriorate could also pose a fire hazard.

Finally, smoking should be forbidden in the storage area of a warehouse, and restricted to designated places.

#### **Theft**

Depending on the types of commodities stored at a warehouse, theft can be a serious problem. It is important to understand the security measures that the warehouse operator has taken to protect the property stored inside.

Entry and exit of customers and employees should be monitored. Customers should be instructed to register at a front office and should be accompanied to their property by a warehouse employee. Employees should punch a time clock or at least sign in when they report to work. Employees should not visit coworkers at the warehouse during time off.

If possible, underwriters should examine the hiring practices of the warehouse operator. Prospective employees should be checked for criminal records as well as employment history. Ideally, the operation will be staffed by long term employees and will have a low turnover of its work force.

The underwriter should be aware of target commodities that are stored at the location and the measures that the warehouse has taken to protect them. Inventories of consumer electronics, finished tobacco products, alcoholic beverages, and personal computer components can increase the exposure to theft.

Underwriters should verify that appropriate protective devices are in place if target commodities are stored. These might include security patrols on the premises, central station premises alarms, lights, and segregated and secured storage areas for target commodities. In lieu of these security measures, underwriters may want to provide a sublimit for these commodities or exclude them from the policy.

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## **Defense Costs**

As well as providing legal liability coverage for stored property, the WOLL also covers costs and expenses that may be incurred in defending a suit against the warehouse operator. This legal action must be the result of alleged loss or damage to property stored at the insured warehouse. The policy provides a defense even if the suit or legal action is fraudulent and groundless.

Warehouse risks that show a frequency of claims should be examined closely. Even if a claim has never been paid, substantial defense costs could easily make the risk unprofitable.

## **Management**

The quality of the management of a warehouse is a key component to underwriting a risk. A warehouse operation's hiring practices, training programs, safety program, and attention to detail has a significant impact on whether a risk will be a profitable.

The potential for shortage or damage to goods stored in a warehouse is directly affected by the quality and training of the insured's employees. Their duties may include strapping goods to pallets, moving the pallets with forklifts, placing pallets on racks and retrieving property for shipment. The storage configuration of a warehouse usually involves various levels of racks. Property may have to be placed on or retrieved from racks which are ten to 12 feet high.

## **Water Damage**

Underwriters should make sure that the warehouse building is in sound condition. The warehouse operator could be held liable for water damage losses that result from leaks in the roof or walls, sewers that back up, and chronic seepage problems.

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## **Earth Movement and Flood**

Earth movement and flood are not excluded perils under the WOLL policy. However, because the WOLL is a legal liability policy, earth movement and flood are not generally considered major perils. However, there may be special circumstances under which the warehouse operator could be found to be legally liable for flood or water damage. A warehouse near a river which floods regularly or causes water backup through sewers should have safeguards to protect against water damage.

## **LOSS CONTROL**

The following is a list of possible questions that can be addressed during a loss control survey.

This list is **NOT** intended to represent a comprehensive and exhaustive treatment of loss control issues that relate to warehouse operators legal liability. **UNDERWRITERS SHOULD CONSIDER** additional questions that address concerns about specific types of operations and/or individual risks.

### **Loss Control Survey**

As well as verifying the information that the underwriter has obtained, the loss control survey should verify the following:

1. condition of the building, and the condition of plumbing and electrical systems;
2. floor area, height in stories, and total area used for storage;
3. adequacy of storage areas for target commodities and flammable goods;
4. comment on the height and condition of storage racks, and whether there is enough space between the highest racks and the ceiling for sprinklers to be effective;

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5. house keeping of the warehouse. Is the storage area neat and orderly, and free of unused pallets, debris, and refuse; and
6. protective systems cited in the application are in place and functional.

## **COLD STORAGE WAREHOUSING**

Cold storage refers to property that must be kept in a storage area where the temperature is controlled. Food and food additives make up the bulk property in cold storage. However, there are warehouses that store chemicals, cleaning supplies, paint, and other non-food items which are temperature sensitive.

Cold storage operations may be part of a greater warehousing operation or may be a completely separate operation. In either case, cold storage is a type of warehousing and from an insurance standpoint holds most of its coverage needs in common with "dry" warehousing.

### **Risk Selection - Cold Storage**

The following information should be obtained to evaluate the condition and adequacy of a cooling system:

1. age of the system and upgrades;
2. installation of temperature alarms;
3. inspection and maintenance schedule, the system should be inspected at least twice a year.

There should be a contingency plan in the event of a cooling system breakdown. A large cold storage operation should have an auxiliary cooling system or generators and employees who are properly trained to use them. The plan should also include telephone or beeper numbers of warehouse supervisors, repair personnel and emergency repair companies.