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## **LIABILITY IN SUBROGATION OF A RESIDENTIAL TENANT TO THE INSURER OF A LANDLORD**

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## **Introduction**

The reality of urban life nowadays is that people are moving from one place to another and changing their living places quite frequently. And probably the simplest way is to rent a house or an apartment. Another common thing is that living residencies are usually insured against fires and other casualties. Thus, we have a landlord of the dwelling, his tenant, and an insurance company that insures the premises. This situation is familiar to the people all around the world as well as to Lithuanians too. But let us assume that the tenant causes the fire in the leased apartment. Supposedly, the insurance company reimburses the landlord for the damages sustained. And, as soon as the insurance company pays the money to the landlord, the question of subrogation arises. Generally, “subrogation means substitution” where one person is substituted in the place of another and succeeds to the latter’s rights in relation to a lawful debt or claim against the third party<sup>1</sup>. Here, the landlord is substituted by his insurer who then seeks to proceed against the tenant. The question of subrogation is important both to the insurer that wants to get back the money paid and to the tenant who probably does not even think that he should pay for his negligence if the premises were insured.

Thus, the main purpose of this article is to answer whether the insurance company can get back the money paid to the landlord from the tenant who is responsible for causing damage to the landlord’s premises. It will be looked at what the general subrogation doctrine says on the issue. Also, the arguments for both sides will be presented and discussed. In finding the arguments the American court cases will be used since this country has a lot of experience in their court practice compared to Lithuania.

The first part of the article will overview subrogation doctrine in general, its history and its purposes for better understanding what principles govern the issue at question. The second part will describe what the participating parties are. This is important because the connection and behavior of the parties might determine whether a subrogation question arises at all. The third part will look at the lease between the landlord and the tenant; the reader will see that this is essential in finding an answer to the raised question. It will be shown how important is to clearly draft the lease concerning the tenant’s liability. Also the arguments will be presented for and against the tenant’s liability when the lease does not expressly state that. The fourth part will discuss how the tenant’s liability changes when his acts are considered intentional, as opposed to negligent. And finally, the fifth part will briefly describe the situation in Lithuania and will answer why the practice on this particular issue is really poor.

### **1. Subrogation**

Generally, under the doctrine of subrogation “if A owes a debt to B, and C pays that debt under some form of legal compulsion, i.e. not as a volunteer, C becomes entitled to bring B’s cause of action against A to recover the amount paid”<sup>2</sup>. “This transfer of responsibility is accomplished by the fiction that the paying party (subrogee) steps into the shoes of the party who suffered the loss (subrogor)” and gets the possibility to enforce the

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<sup>1</sup> John J. O’Brien, *Distinct Subrogation Issues: Pandora’s Box*, <[www.subrogation.net/edu/edu2.doc](http://www.subrogation.net/edu/edu2.doc)>, visited 2002 03 30.

<sup>2</sup> John F. Dobbyn, *Insurance Law in a Nutshell*, (St. Paul (Minn.): West Group, 1996), p. 282.

latter's rights against the responsible person.<sup>3</sup> The Lithuanian Law is also familiar with this doctrine; a separate chapter of the Civil Code of Lithuania is devoted to the subrogation.<sup>4</sup>

In the context of insurance subrogation is defined in the following way: Subrogation - the right of an insurer to recover from a third party who is wholly or partially responsible for a claim paid or payable by an insurer<sup>5</sup>. Similarly, the Lithuanian Civil Code in its Insurance Chapter says that "an insurer after paying the proceeds gets a right to require the paid sums from the person who is at fault".<sup>6</sup> It also has to be remembered that the general rule is that "an insurer acquires no right of subrogation until it has paid a loss"<sup>7</sup> to the insured.

### *1.1. Conventional and Equitable Subrogation*

There are two ways how subrogation rights arise: by contract or by operation of law. The one, which arises by contract, is called conventional subrogation, the other - equitable.<sup>8</sup>

Conventional subrogation arises when an insurance policy contains special provision by which a right to subrogation is expressly granted to the insurer.<sup>9</sup> Usually, a typical contract of insurance has a subrogation clause like that:

*In the event of any payment under this policy, the Company shall be subrogated to all insured's rights of recovery therefore against any person or organization and the insured shall execute and deliver instruments and papers and do whatever is necessary to secure such rights.*<sup>10</sup>

A right to equitable subrogation arises "when there is no actual contractual language granting a right to subrogate"<sup>11</sup>.

There is a lot of debate concerning those two ways of subrogation: it is argued whether equitable subrogation can still be available when the contract does not have any provisions concerning subrogation. Although the opinions differ, some kind of a general rule seems to exist, as John Dobbyn in his book "Insurance Law" states:

*...subrogated rights arise in the insurer by action of law, regardless of whether or not they are provided for in the insurance contract or in any transactions between the insured and third party*<sup>12</sup>.

Thus, if an insurance contract does not expressly provide for subrogation, the insurer could still sue the tenant as an equitable subrogee. Why this is so could be probably

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<sup>3</sup> Gregory R. Veal, "Subrogation: the Duties and Obligations of the Insured and Rights of the Insurer Revisited", *ABA Tort & Insurance Law Journal* (Fall 1992) <www.lexis.com>, visited 03 22 2003.

<sup>4</sup> LR Civilinis Kodeksas, (2000 07 18, Nr. VIII- 1864), 6 Knyga, I Dalis, VII Skyrius: Reikalavimo Perėjimas Trečiajam Asmeniui Regreso Tvarka (Subrogacija).

<sup>5</sup> John Owen Clark, *International Dictionary of Insurance and Finance* (Chicago, IL: Glenlake, 1999), p. 16.

<sup>6</sup> See footnote 4: author's translation from LR Civilinis Kodeksas, 6 Knyga, IV Dalis, LIII Skyrius: Draudimas, Art. 6.1015, Part 1.

<sup>7</sup> Andrew C. Hecker, Jr., "Subrogation - Potential Defenses", *ABA Tort & Insurance Law Journal* (Summer 1983) <www.lexis.com>, visited 03 22 2003.

<sup>8</sup> See note 3: Gregory R. Veal.

<sup>9</sup> Eric J. Pickar, "Westfield Insurance Company, Inc. v. Rowe: The South Dakota Supreme Court Rejects the Common Law "Made Whole" Doctrine on a Property Insurance", *South Dakota Law Review* (2002, 47 S.D.L. REV. 316) <www.lexis.com>, visited 2002 03 22.

<sup>10</sup> See note 1: John O'Brien.

<sup>11</sup> See note 9: Eric J. Pickar.

<sup>12</sup> See note 2: John Dobbyn, p.282.

answered looking at the general purposes of subrogation and to the history where it came from.

### *1.2 Purposes of Subrogation*

Subrogation rights arise from the common law doctrine of equity; equity is the English legal system that stresses natural justice as the superior principle.<sup>13</sup> “The equity side of the courts strove to right “wrongs” and to follow the natural law”,<sup>14</sup>

So, in insurance under equitable principles it is sought to indemnify the insured for his losses – that is why the property insurance contract is considered indemnification contract.<sup>15</sup> But if an insured after getting money from the insurance company also gets money from the third party tortfeasor, this will be double indemnity, which offends natural justice. Thus, the purpose of subrogation is to prevent double recovery of the insured.<sup>16</sup>

Another purpose of subrogation is to make the party who is responsible to pay for the damage it has done. This prevents a third party tortfeasor to get away without paying, since the situation might arise when the insured after getting reimbursed from his insurer may not want to sue the tortfeasor and go through the litigation proceedings; this would be both unfair and against public policy.<sup>17</sup>

## **2. Tenant. Landlord. Insurer**

Whether the right to subrogation arises depends both on the insurance contract (which is governed by the insurance law) and on the lease (which is governed by the lease contract law). Thus, those two different branches of law become interconnected when solving the subrogation problem.

First, the landlord has to get insurance money from the insurer for a right of subrogation to arise. It looks like he is entitled to the money because of the insurance contract that has to indemnify the insured. However, before paying, the insurer considers the lease contract between its insured landlord and his tenant. There may be instances where the lease’s provisions might preclude the landlord from getting paid, like, for example, when the landlord releases the tenant from liability having no right to do that.<sup>18</sup>

Thus, if the insurer does not pay to the landlord he gets no right of subrogation. In this case, the analysis has to stop right there since the further possible actions of the parties are behind the scope of this article.

But let us assume that the landlord gets paid. Then, according to the general rule, the insurer after paying to the landlord should be subrogated to his rights to require the amount paid from the tenant who caused the damage.<sup>19</sup> Thus, we are left only with the tenant and the insurer since the landlord steps aside after being reimbursed. But, again, the insurer has only those rights against the third party that his insured, here the landlord, had.<sup>20</sup> This

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<sup>13</sup> John O’Brien, “The Origins of Subrogation”, <[www.subrogation.net/edu/edu1.doc](http://www.subrogation.net/edu/edu1.doc)>, visited 2003 03 30.

<sup>14</sup> *Id.*

<sup>15</sup> <[www.pittslaw.com/eight.htm](http://www.pittslaw.com/eight.htm)>, visited 2003 03 23.

<sup>16</sup> See note 2: John Dobbyn, p.284.

<sup>17</sup> *Id.*

<sup>18</sup> See part 3.1 of this article for more.

<sup>19</sup> See note 2: John Dobbyn, p. 282.

<sup>20</sup> See note 2: John Dobbyn, p. 283.

evolves out of the general doctrine of subrogation which was mentioned earlier - the subrogee by stepping into the shoes of the subrogor is entitled to bring subrogor's cause of action, and this means that if subrogor does not have a right of action against the third party, the subrogee does not have this right either. Thus, what should be considered once again is the lease because this is the contract where the landlord and the tenant set their rights and obligations.

### ***3. Landlord - Tenant Relationship Established by the Lease***

First thing that should be done in deciding the tenant's liability before the insurer of the landlord is the careful examination of the lease contract. That is because as it was stated above the insurer after stepping into the shoes of the landlord has only those rights, which the landlord had against the tenant. Thus, if after reading the lease it is clear that the landlord would be able to sue the tenant it means the insurer also can do this.

#### *3.1 Lease Containing Express Statement Concerning the Tenant's Liability*

The best way to avoid future misunderstanding and litigation is to clearly state the parties' responsibilities in the lease since "tenants and landlords are always free to allocate their risks and coverage by specific agreements, in their leases or otherwise"<sup>21</sup> as to insurance and liability. As it will be seen in the next subsection most problems occur when it is not clear from the lease whether the tenant is liable for the damages or is released from liability. In such cases the court has to interpret the contract and this does not mean that it will be interpreted correctly, since the courts come to completely different conclusions in similar situations. Thus, if the lease contains a clause making the tenant specifically liable for the damages caused to the landlord's property, no matter intentionally or negligently, the landlord's insurer after paying to the landlord will be able to bring subrogation claim against the tenant.<sup>22</sup>

On the other hand, the lease may contain a release provision where the tenant is expressly released from liability to the landlord, in that case the insurer would probably be barred from maintaining a subrogation action against the tenant because, as mentioned earlier, after stepping into the shoes of his insured he has no greater rights than the insured had. But this is only valid when the landlord releases the tenant "prior to entering into the insurance contract" with the insurer.<sup>23</sup> However, if the landlord releases the tenant "after the contract of insurance is entered into (at which time the right of subrogation automatically attaches) he will be held to have breached his contract with the insurer, thus presenting the insurer with a defense against payment of any claims under the policy"<sup>24</sup>. The tenant in this situation would probably go free, because even that the landlord did not get paid by the insurer, he would not be able to recover from the tenant either since the tenant has a release.

The third possible situation is that the landlord releases the tenant after the loss and after getting paid from the insurer. Then there are two possibilities in regard with the tenant's liability in subrogation: first, if the tenant in obtaining the release knew of the landlord's insurer's rights, the release would not be valid and the insurer could sue the

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<sup>21</sup> *Dilullo v. Joseph*, 259 Conn. 847; 2002 Conn.

<sup>22</sup> Seth Emmer, "Subrogation Claims Involving Tenants",  
<[www.meeb.com/articles/subrogation\\_claims.htm](http://www.meeb.com/articles/subrogation_claims.htm)>, visited 2003 04 02.

<sup>23</sup> See note 2: John Dobbyn, p. 283.

<sup>24</sup> *Id.*

tenant in subrogation; secondly, if the tenant had no knowledge about the insurer's rights the release would be a defense against the insurer's subrogation action.<sup>25</sup>

The next part will show how important is to draft the lease carefully because there are instances of cases where the lease contains nothing express that would relieve the tenant from liability but the courts still tend to interpret the lease in favor of the tenant and find an implied release.

### 3.2 Lease with no Express Statement about the Tenant's Liability

It is not always clear from the lease who is responsible for the damages to the premises. In the cases where there is no express statement that the tenant would be liable in case of damaging the landlord's property and the other provisions of the lease do not clear this up it is left to the courts to decide whether the tenant is liable. In deciding the question American courts have gone into two opposite directions: the first saying the tenant is liable and the others refusing subrogation to the insurer against the tenant. The coming sections will discuss the arguments of both sides.

#### 3.2.1 Arguments in Favor of the Tenant

The courts favoring the tenant's position come to conclusion that absent an express agreement establishing tenant's liability the insurance obtained benefits both the landlord and the tenant, thus, the tenant becomes the co-insured and not liable to the insurer of the landlord.<sup>26</sup>

Nevertheless, first thing that the courts try to do when faced with this question is to try to find out the real intent of the parties at the time the lease was signed, because "as a matter of the traditional rules of contract law, whether subrogation would or would not apply ordinarily would depend, in large part, on a case-by-case analysis of the language of ... leases involved"<sup>27</sup>. One of the early American cases *Cerny-Pickas v. Jahn*.<sup>28</sup> illustrates the issue. There the tenant negligently caused the fire to the leased premises. The lease did not contain any express provision that the lessee would or would not be liable for damages resulting from his own negligence. The Court agreed that "if the lease contained such an express provision, that would be the end of the matter"<sup>29</sup>, however, it also recognized that the lease should be viewed as a whole and it could still be shown that "the parties themselves intended that the lessee should not be liable"<sup>30</sup>.

What the lease contained was:

*... Lessee will keep said premises, including all appurtenances, in good repair, ... and upon the termination of this lease, in any way, will yield up said premises to Lessor in good condition and repair (loss by fire and ordinary wear excepted)...*

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<sup>25</sup> Id.

<sup>26</sup> John Dwight Ingram, "Should an Illinois Tenant Get the Benefit of the Landlord's Insurance?", *The Northern Illinois University Law Review*, (Fall 1996), <www.lexis.com>, visited 2003 03 22.

<sup>27</sup> See note 21: *Dilullo v. Joseph*.

<sup>28</sup> *Cerny-Pickas v. Jahn*, 7 Ill. 2d 393; 1955 Ill.

<sup>29</sup> Id.

<sup>30</sup> Id.

*...the Lessee at his own expense will keep all improvements otherwise in good repair (injury by fire, or other causes beyond Lessee's control excepted)...*

*...Lessor shall pay for fire insurance on the building...*<sup>31</sup>

Looking at these particular provisions the Court found that the intent of the parties was to look only to the lessor's insurance because he took an obligation to pay for the insurance and loss by fire was excepted as to the tenant's keeping of the premises, thus relieving the tenant from liability. This does not really seem very persuasive since the provisions of the lease are pretty ambiguous as to the tenant's liability for fire in this case.

Another case that concentrated on the parties' intent was *Dix Mutual v. LaFramboise*.<sup>32</sup> There the tenant also negligently caused the fire. The Court's finding was that even if the lease does not expressly state the tenant's liability the court can still find that the intent of the parties was to relieve him from liability. The relevant provision of the lease was that the tenant would assume his own risk for his personal property and the landlord would not be responsible for fire, wind, or water damage.<sup>33</sup> The Court found that this provision only showed that in the case of the event the landlord would not be responsible for damages to the tenant's property, thus, the parties would be responsible for their own property.<sup>34</sup> So, it comes out that if the lease does not reflect the intent that the tenant would be responsible for the damages he will not be liable. It looks like the Court really favors the tenant since the lease does not actually reflect the landlord's intent to be responsible for the damages caused by the tenant either. The Court cites a lot from the *Cerny-Pickas* case that was discussed above, but here the lease does not even contain a provision that the landlord would provide fire insurance.

Thus, looking at the provisions of the leases, the real intent of the parties is not clear, and most probably the landlord would be allowed to sue the tenant if he had no insurance. But in this case the courts seem not to adhere to the rule that the subrogee gets all the rights of the subrogor and do not let the insurer to bring an action against the tenant. Of course, this nonobservance is supported by other arguments not only interpretation of the lease in favour of the tenant. Like, for example, the court in a *Stein v. Yarnall*<sup>35</sup> case with a similar fact situation as in *Cerny-Pickas* leaves aside the analysis of the lease and uses another argument in support of the tenant looking at the situation from the perspective of practical inconvenience (also citing from *Cerny-Pickas*):

*Under the construction urged by the lessor it would be necessary for both parties to the lease to carry fire insurance if they are to be protected. The lessee would have to insure against fires due to his negligence, and the lessor against fires due to other causes. ... It would be a tortured construction, indeed, to say that under the lease here it was proposed that the lessor would procure fire insurance to cover fire risks save those which might be attributable to the negligence of the lessee or its employees. Under such a construction the lessee, to protect itself, then would seek an unusual, if not unique, policy to cover the risk of its own negligence, but nothing more.*<sup>36</sup>

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<sup>31</sup> Id.

<sup>32</sup> *Dix Mutual v. LaFramboise*, 149 Ill. 2d 314, 1992 Ill.

<sup>33</sup> Id.

<sup>34</sup> Id.

<sup>35</sup> *Stein v. Yarnall-Todd Chevrolet, Inc.*, 41 Ill. 2d 32.

<sup>36</sup> Id. Also see note 28: *Cerny-Pickas v. Jahn*.

In the protection of the tenant this argument was developed even further in the recent case *Dilullo v. Joseph*.<sup>37</sup> The court reasoned it's opinion that the sufficient insurance the tenant would be required to get if the rule was that he is liable absent express agreement to the contrary, would be economically wasteful:

*Such a rule would create a strong incentive for every tenant to carry liability insurance in an amount necessary to compensate for the value, or perhaps even the replacement cost, of the entire building, irrespective of the portion of the building occupied by the tenant. That is precisely the same value or replacement cost insured by the landlord under his fire insurance policy. Thus, although the two forms of insurance would be different, the economic interest insured would be the same. This duplication of insurance would ... constitute economic waste, in a multiunit building, the waste would be compounded by the number of tenants.*

Besides this "economic waste" argument there is one more that the negligent tenants could use in trying to escape liability to the insurer. *Cerny-Pickas* court indulged "in a legal fiction",<sup>38</sup> assuming that the lessor in deciding the cost of the rent always adds in the cost of the insurance, so, practically this means that it's the tenant who actually pays for the insurance<sup>39</sup>. The Court in *Dix Mutual* also took this idea to conclude that "the tenant, by payment of rent, has contributed to the payment of the insurance premium"<sup>40</sup>:

*The ancient law has been acquiesced in, and consciously or unconsciously, the cost of insurance to the landlord, or the value of the risk enters into the amount of rent. ... They necessarily consciously figured on the rentals to be paid by the tenant as the source of the fire insurance premiums and intended that the cost of insurance was to come from the tenants. In practical effect the tenant paid the cost of the fire insurance.*<sup>41</sup>

The leading case in the tenant's defense is *Sutton v. Jondahl*<sup>42</sup>. The facts were that the property was damaged by a fire caused by the tenant's 10-year-old son, who was playing with a chemistry set. Here the court also denied the insurer of the landlord subrogation action against the tenant. The court heavily relied on the fact that the landlord did not require the tenant to purchase the fire insurance but instead did this himself. Just like in the other cases cited above, it has also assumed that it was the tenant who had actually paid for the insurance in the way that the landlord charged this sum from him in counting the cost of the rent.<sup>43</sup>

But actually what this case is famous about is that it created a so called "Sutton" doctrine under which the tenant is considered to be a co-insured under the landlord's insurance policy if there is no express agreement to the opposite.<sup>44</sup> The main argument of the court was that the tenant is the co-insured because both the landlord and the tenant have

<sup>37</sup> See note 21: *Dilullo v. Joseph*.

<sup>38</sup> *Fire Insurance Exchange v. Geekie*, 534 N.E.2d 1061, 1989 Ill. App.

<sup>39</sup> See note 28: *Cerny-Pickas v. Jahn*.

<sup>40</sup> See note 32: *Dix Mutual v. LaFramboise*.

<sup>41</sup> *Lothrop v. Thayer*, 138 Mass. 466, 475; also see note 32: *Dix Mutual v. LaFramboise*.

<sup>42</sup> *Sutton v. Jondahl*, 532 P. 2d 478, Okla. App. 1975.

<sup>43</sup> *Id.*

<sup>44</sup> John Chernosky, *Insurance Law* (lecture notes, Kaunas, VMU Law School, fall 2002).

an insurable interest<sup>45</sup> in the property and the tenant naturally expects that he is on the safe side because the landlord has insured the premises:

*To suggest the fire insurance does not extend to the insurable interest of an occupying tenant is to ignore the realities of urban apartment and single-family dwelling renting. Prospective tenants ordinarily rely upon the owner of the dwelling to provide fire protection for the realty (as distinguished from personal property) absent an express agreement otherwise. Certainly it would not likely occur to a reasonably prudent tenant that the premises were without fire insurance protection or if there was such protection it did not inure to his benefit and that he would need to take out another fire policy to protect himself from any loss during his occupancy. Perhaps this comes about because the companies themselves have accepted coverage of a tenant as a natural thing. Otherwise their insurance salesmen would have long ago made such need a matter of common knowledge by promoting the sale to tenants of a second fire insurance policy to cover the real estate.*<sup>46</sup>

Thus, in stating that the tenant also has an insurable interest the Court puts him in totally different position compared to the third party tortfeasor who in the doctrine of subrogation would be responsible to the insurer of the landlord. Thus, considering the tenant “a joint owner”<sup>47</sup> means that he is also protected by the insurance policy since this is “basic equity and fundamental justice upon which the equitable doctrine of subrogation is established”.<sup>48</sup> And this argument certainly precludes the insurer against bringing subrogation claim against the tenant.

All the above mentioned arguments are used to exonerate the tenant from liability against the insurer of the landlord. Basically, the tenant’s side sets “a default rule”<sup>49</sup> that the tenant cannot be liable in subrogation unless there is an express agreement to the contrary. The next section will be dealing with the counter-arguments, that is, with the arguments to let the insurer to bring the subrogation action against the tenant and to defeat the arguments just mentioned.

### 3.2.2 Arguments in Favor of the Insurer of the Landlord

This side is of completely different opinion and tries to show that the landlord’s insurer may bring a subrogation claim against the tenant unless there is an express agreement in the lease to the contrary.

One of the cases supporting this theory is *Fire Insurance Exchange v. Robert Geekie*.<sup>50</sup> The fact was that while the tenant was repairing his car in the garage of the leased premises, a fire damaged the premises. There was no written lease at all; the landlord was a son who orally leased the house to his father. The court was of the opinion that in the cases like this nothing suggests that the landlord’s intent was to exonerate the tenant from

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<sup>45</sup> A person has an insurable interest in a subject matter where he has a concern in such subject matter that he will derive pecuniary damage by happening of the event insured against. Id.

<sup>46</sup> See note 42: *Sutton v. Jondahl*.

<sup>47</sup> Id.

<sup>48</sup> Id.

<sup>49</sup> See note 21: *Dilullo v. Joseph*.

<sup>50</sup> See note 38: *Fire Insurance Exchange v. Geekie*.

liability.<sup>51</sup> The tenant cannot be considered a co-insured because, under the court's opinion, a traditional landlord-tenant law should apply "which holds the tenant responsible for his own negligence".<sup>52</sup> Such a privilege of being a co-insured should be expressly stated in a lease or in the insurance contract. The court's reasoning goes hand in hand with the equitable principles out of which the doctrine of subrogation evolved, which says that the third party tortfeasor should pay for the damages it causes and should not get the windfall because the insurer pays to the landlord.<sup>53</sup> In supporting this idea the court at the same time criticizes those who tend to interpret the leases in favor of the tenant:

*...law supports a tenant's right to contract in his lease agreement to shift the burden of the loss suffered as a result of his negligently caused fires. When the landlord and tenant have not included in their contract a term shifting the burden, however, a court should not indulge in a legal fiction to create such a term and alter the parties' contract.*<sup>54</sup>

Really, in the cases that support tenant's position, the courts used to "indulge in a legal fiction" and find intent of the parties to relieve the tenant from liability where there was no express statement in the lease about that. Let us return to one of such cases that was already discussed above, that is, *Dix Mutual Insurance Company v. LaFramboise*.<sup>55</sup> The dissent there, unlike the majority of the court, found no intent of the parties to exonerate the tenant from liability. In the lease the tenant assumed his own risk for his personal property and the landlord refused responsibility for fire, wind, or water damage.<sup>56</sup> This only relieved the landlord from liability to the tenant's property, but it could not be logically figured out that the same provision relieved the tenant from liability for damaging the landlord's property.<sup>57</sup>

The dissenting judge also criticized the idea that the tenant actually pays for the insurance by saying that this "assumption is as gratuitous as saying that the payment of rent included maid service and clean linens".<sup>58</sup> To tell the truth, it could be easily agreed with this argument since in agreeing that the tenant pays for the insurance it could then also be said that he pays for other things, such as "taxes, interest on loans, janitor, premiums on other insurance policies of the landlord, etc." and if that would be so, the tenant would probably have a right to require from the landlord to share the benefits with him in proportion that he paid in as a part of the rent.<sup>59</sup>

The counter-argument against holding the tenant a co-insured can also be found in the *Dix Mutual* case by the dissenting judge Heiple. Here the judge explains why the tenant should not be held a co-insured under the landlord's insurance policy:

*There is nothing in law to require an insured to look either first or only to his insurance carrier for recovery of loss caused by another's negligence. The landlord, in this case, could have sued the tenant directly. There is also nothing in law to require a landlord to carry fire insurance at all. How can it be said that a tenant is deemed to be a co-insured in a lease when the lease does not even mention or contemplate insurance? Suppose that the landlord in this case had not taken out an insurance policy. Would the majority say he was debarred*

<sup>51</sup> Id.

<sup>52</sup> Id.

<sup>53</sup> This is one of the purposes of subrogation doctrine as mentioned in part 1.3 of this article.

<sup>54</sup> See note 38: *Fire Insurance Exchange v. Geekie*.

<sup>55</sup> See note 32: *Dix Mutual v. LaFramboise*, also see part 3.2.1. of this article.

<sup>56</sup> Id.

<sup>57</sup> Id.

<sup>58</sup> Id.

<sup>59</sup> See note 26: John Dwight Ingram.

*from suing his tenant for negligently burning down the premises? That is to say, would the loss be shifted away from the negligent tenant and onto the guiltless landlord?*<sup>60</sup>

This is also a very good argument because the landlord would be allowed to sue the tenant and the doctrine of subrogation says that the party who pays for the losses to a person gets all the rights of that person, thus there is no reason why the insurance company should not get the right to sue the tenant.

Those who hold the tenant the co-insured under the landlord's policy draw this conclusion out of the idea that the tenant just like the landlord has an insurable interest in the leased property. This is a mistake because only the lessor has an insurable interest in the property, what the lessee has is possessory interest, that is what he may lose because of the loss of use of the leased property.<sup>61</sup> If the property is damaged, only the landlord derives pecuniary damage from the loss of the property that belongs to him.

The argument that if the tenant is not protected by the landlord's insurance he would have to buy his own insurance for the building what would result in double payment to the insurance companies can also be easily defeated using the same theory of the insurable interest - if the tenant does not have an insurable interest in the property he does not have a reason to purchase an insurance policy on that property, except to the extent that damage to the premises would cause some loss to him connected with the tenant's loss of use of the leased premises.<sup>62</sup> In this case the only thing the tenant needs to be on the safe side is liability insurance:

*As to the risk of damage to the landlord's ownership interest in the building, the tenant's only exposure to loss is the possibility that the tenant's negligence will be the cause of damage to the building. This is a normal, everyday third-party liability exposure, which is covered by the tenant's own liability insurance coverage, most commonly included in the renter's package policy covering his own personal property, his loss of use, and his risk of liability for damage to the person or property of others. Every prudent tenant should have liability insurance, and therefore has no need to buy insurance on the building itself, in which the tenant has no insurable interest anyway.*<sup>63</sup>

All of the arguments stated in the last two sections support two opposite sides concerning the tenant's liability to the insurer of the landlord absent express statement about this in the lease contract. Yet, it can be said that the final word is still on the court and as we saw the courts tend to break general principles of subrogation and find arguments to refuse subrogation against the tenant. Thus, the easiest way to avoid litigation and problems on this issue is a careful drafting of the leases, because the law allows both parties of the contract to agree on the lease provisions concerning liability and insurance.

#### ***4. Intentional and Negligent Acts of the Tenant***

The cases discussed in the previous chapter were dealing with the negligent tenants. In these cases the courts sometimes hold the tenant a co-insured and relieve him from

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<sup>60</sup> See note 32: *Dix Mutual v. LaFramboise*.

<sup>61</sup> See note 26: John Dwight Ingram.

<sup>62</sup> *Id.*

<sup>63</sup> *Id.*

liability in subrogation. This part discusses whether the tenant acting intentionally could escape liability.

There is no question that if the tenant is not deemed a co-insured he is liable in subrogation anyway. In the situation where the tenant is expressly or by implication considered a co-insured he gets the same protection against the insurer's subrogation claim as the insured. And under the general doctrine of insurance the insurer only acquires the rights of its own insured and cannot go in subrogation after him.<sup>64</sup> This also means that the insurer cannot go after the co-insured tenant.<sup>65</sup> Yet, another general rule is that subrogation is allowed for the intentional acts of the insured<sup>66</sup>, this is because, as mentioned above, subrogation is intended to place the burden of loss on the third party who is at fault. Here the tenant is responsible and while perhaps deemed a co-insured, any benefits of that status are lost since he intentionally damaged the landlord's property and if the landlord is paid by the insurer, fairness and justice require the right of subrogation to permit the insurer to proceed against the tenant. Besides, the insurance companies usually have the exception for intentional acts of their insureds in the insurance policies to deny coverage, or in the case of the tenant to sue him in subrogation.

### 5. Lithuanian Experience

Lithuanian laws in the sphere of subrogation in insurance are still developing. So far there are no court cases on the issue particularly involving tenants and landlords. Probably the practice used by Lithuanian insurance companies may answer the question why this does not even come to subrogation. For example, one of the biggest insurance companies "Lietuvos draudimas"<sup>67</sup> tends to look at the tenant and at the landlord as at one and the same person.<sup>68</sup> The explanation is as follows, The Law of Insurance of 1996 used to have a provision:

*The insured shall also be held responsible for breach of a contract of insurance in those instances when obligations arising from the implementation of a contract of insurance are violated by persons ... residing with the insured.*<sup>69</sup>

Later this was changed and it was left for the insurance contract parties to decide on their duties and obligations.<sup>70</sup> And most of the insurance companies now have something similar in their internal rules governing the insurance of property, like "definition of the insured also includes his family members and persons legally residing with him".<sup>71</sup> Thus, the companies tend to hold a tenant "a person residing together with the landlord". Then, it comes out that whenever a tenant causes damage that is within a definition of a breach of the insurance contract, it is the same as if the landlord has done it, and in this case the

<sup>64</sup> *Alaska Ins. Co. v. RCA Alaska Communications*, 623 P.2d 1216 (Alaska 1981).

<sup>65</sup> *Id.*

<sup>66</sup> Tracy Stevenson, "Landlord or Tenant- Who Pays for the Tenant's Negligence?" <[www.insurancefraudlaw.com](http://www.insurancefraudlaw.com)>, visited 2002 04 12.

<sup>67</sup> "Lithuanian Insurance".

<sup>68</sup> Giedrius Tunkevičius, interviewed by the author, 2002 05 05.

<sup>69</sup> Official text with changes until 1996 07 31, Žin. (1996 Nr.73-1742), Žin. (1996 Nr.125 (atitaisymas)), Art. 12, Part 3. Official translation: <[www.lrs.lt](http://www.lrs.lt)>, visited 2002 04 10.

<sup>70</sup> Draudimo įstatymo antrojo skirsnio pakeitimo ir įstatymo papildymo 70 straipsniu Įstatymas, (in force from 2002 03 20), Žin. (2002 Nr.29-1033).

<sup>71</sup> Author's translation from "Namų turto draudimo taisyklės" (ERGO, NTDT, 2002), <[www.ergo.lt/file/1268](http://www.ergo.lt/file/1268)>, visited 2002 04 17.

insurer does not pay to the landlord. Thus, a right to subrogation does not arise at all since, as already mentioned, this is a general rule of subrogation. Similarly, it should mean that if the tenant is only negligent and he is considered the same person as the landlord, the landlord should be reimbursed with no right for insurance company to sue the tenant in subrogation. But, in the author's opinion, such interpretation is erroneous because the tenant cannot be considered as living together with the landlord. This is simply because persons living together with the landlord are sharing a right of use of the residence with the landlord; but what concerns the lease, usually all the rights of use and possession are transferred from the landlord to the tenant.<sup>72</sup> The tenant could even ask the landlord out if he does not prefer his company. Yet, on the other hand, if the lease is oral, the landlord can simply lack evidence to prove that the tenant was "a tenant" but not "a person residing together".

Whatever is the case, if it gets to the Lithuanian court and the court clears this definition out, insurers would probably start paying to the landlords and then would seek to sue the tenants in subrogation. In that case, the American experience would probably be helpful both for insurers and the tenants.

### *Conclusions*

As we have seen, it is not always adhered to the general principle of subrogation, which allows the insurer after stepping into the shoes of it's insured to sue the third party at fault, which is a tenant in our case. Although there are certain instances when it is clear that the tenant would be liable to the insurer of the landlord, like when it is clearly stated in the lease or when the tenant's acts qualify as intentional. However, when the tenant is only negligent and the lease is silent or it's provisions are ambiguous what concerns tenant's liability, the best answer to the question probably is "it depends", because courts' opinions are split on this question: the first say that the tenant is liable absent an express agreement to the contrary and the other say that he is not unless there is an agreement. The tenant's side's arguments could be summed up in the following way:

1. The tenant actually pays for insurance because the landlord usually adds this money into the cost of the rent.
2. The tenant has reasonable expectations that he will not be liable if the premises are insured.
3. It would be economically wasteful to require both the landlord and the tenant to purchase insurance for the same building.
4. The tenant just like the landlord has an insurable interest in the premises, thus he should be deemed a co-insured.

Another side thinks that the tenant should be liable and use the following counter-arguments:

1. It can not be said that the tenant actually pays for the insurance because if this was so, it could be said that he pays for other things and is entitled to the benefit the landlord gets, such as interest on loans for instance.
2. The landlord could be able to sue the tenant directly for the damages but if we preclude the insurer that substitutes the landlord to sue the tenant, it could be said that the landlord is also debarred from suing the tenant if he would not have taken out an insurance policy.

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<sup>72</sup> See note 4: LR Civilinis Kodeksas, 6 Knyga, I Dalis, XXXI Skyrius: Gyvenamosios Patalpos Nuoma, Art. 6.576.

3. The tenant does not have an insurable interest in the premises, he only has a possessory interest, and this means that he does not need to obtain the same kind of insurance as the landlord. He only needs liability insurance.

Although the latter arguments seem more reasonable because the tenant is still the third party tortfeasor who should be responsible for what he had done, the final answer is on the court, thus the best way to avoid litigation is to clearly state the parties' responsibilities in the lease. However, one thing that most of the courts agree on is that the question is fact dependent and first of all it should be solved on a case-by-case basis, like it was said in one of the early American cases on subrogation:

*The principle of subrogation was begotten of a union between equity and her beloved—the natural justice of placing the burden of bearing a loss where it ought to be. Being so sired this child of justice is without the form of a rigid rule of law. On the contrary it is a fluid concept depending upon the particular facts and circumstances of a given case for its applicability. To some facts subrogation will adhere—to others it will not.*<sup>73</sup>

What concerns Lithuania, the sphere of subrogation is still under formation and the particular question concerning tenant's liability to the insurer has not been raised yet in courts because of erroneous policy of the insurance companies which does not regard the tenant as the third party. But as soon as the question reaches the court American practice should be helpful.

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<sup>73</sup> *Home Owners' Loan Corporation v. Parker*, 181 Okl. 234, 73 P. 2d 170 (1937).

*Abstract in Lithuanian*

**Monika Volkovaitė**

**AR GALI BŪSTO NUOMININKAS BŪTI ATSAKINGU BŪSTO SAVININKO DRAUDIKUI SUBROGACIJOS TVARKA UŽ PADARYTUS NUOSTOLIUS?**

*Santrauka*

Bendroji prasme, subrogacija reiškia vieno asmens pakeitimą kitu. Šis pasikeitimas įvyksta tada, kai teisiškai įsipareigojęs asmuo apmoka kitam asmeniui jo patirtus nuostolius ir perima pastarojo reikalavimo teisę į nuostolių atlyginimą iš trečiųjų asmenų, kurie ir yra kalti dėl patirtų nuostolių. Draudimo srityje, draudikas (draudimo kompanija), apmokėjęs nuostolius draudėjui (apsidraudusiajam), įgauna teisę juos išsireikalauti iš kaltų asmenų. Tačiau, draudikas neįgauna daugiau teisių, nei jų turėjo draudėjas. Mūsų nagrinėjamoje situacijoje draudėjas yra būsto savininkas, o sukėles nuostolius tretysis asmuo yra šio būsto nuomininkas. Vienas subrogacijos tikslų yra neleisti kaltajam asmeniui išsisukti nuo atsakomybės, taigi, nuomininkas turėtų būti atsakingu savininko draudikui. Tačiau teismai ne visada paiso šios taisyklės. Žinoma, tam tikrais atvejais nuomininkas tikrai bus atsakingas savininko draudikui. Vienas tokių atvejų yra kai nuomininko atsakomybė už padarytus nuostolius yra numatoma nuomos sutartyje. Tokiu atveju, draudikas „įlipęs į draudėjo batus“, turės teisę reikalauti iš nuomininko atlyginti nuostolius, nes savininkas šią teisę būtų turėjęs. Kitas atvejis yra kai nuomininkas nuostolius sukelia tyčia, tada jis taipogi būtų atsakingas savininkui, o tuo pačiu ir savininko draudikui subrogacijos tvarka. Tačiau, kai nuomininkas yra tik neatsargus ir, be to, nuomos sutartis nenumato nuomininko atsakomybės arba yra neaiški šiuo klausimu, teismų nuomonė nebesutampa. Lietuvos teismų praktikoje nėra bylų konkrečiai šiuo klausimu dėl klaidingos draudimo kompanijų politikos, kuri draudimo tikslais savininką ir nuomininką traktuoja kaip vieną asmenį (taigi, iki subrogacijos net neprieinama), todėl straipsnyje remiamasi Amerikos teismų praktika, kuri yra ganėtinai plati. Viena teismų pusė palaiko nuomininką ir vadovaujasi nuostata, kad jis nėra atsakingas savininko draudikui, jei sutartyje nenumatyta kitaip. Jų argumentai yra sekantys:

1. Iš esmės, nuomininkas pats moka draudimo kompanijai, nes savininkas, apskaičiuodamas nuomos mokestį, paprastai į bendrą sumą įskaičiuoja ir draudimo išlaidas.
2. Nuomininkas natūraliai tikisi, kad jam nereiks mokėti už padarytus nuostolius jei būstas yra apdraustas.
3. Būtų ekonomiškai nenaudinga versti ir savininką, ir nuomininką įsigyti draudimą tam pačiam būstui. Tai būtų dvigubas mokestis už tą patį draudimą.
4. Nuomininkas, kaip ir savininkas, turi draudiminį interesą<sup>74</sup> į nuomojamą būstą, todėl jis įgyja visas apdraustojo teises.

Kita teismų dalis palaiko draudiką ir mano, kad nuomininkas turi atsakyti subrogacijos tvarka, nebent sutartis numato priešingai. Jų argumentai yra:

1. Negalima sakyti, kad nuomininkas apmoka draudimo išlaidas, nes priešingu atveju būtų galima teigti, kad dalis jo nuomos tenka ir visiems kitiems dalykams, iš kurių savininkas gauna naudą, kaip pavyzdžiui kredito palūkanos.

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<sup>74</sup> Angl. “Insurable interest”.

2. Jei nuomininkas būtų pripažintas neatsakingu savininko draudikui, kuris šiuo atveju pakeičia savininką, tai vadinasi, jei nebūtų draudiko, galima būtų teigti, kad jis neatsakingas ir savininkui, kas prieštarauja sveikai logikai.
3. Nuomininkas neturi draudiminio intereso į būstą, nes jis nepatiria piniginių nuostolių jei būstui kas nors nutinka. O kadangi jis neturi draudiminio intereso, tai jam nereikia drausti šio būsto, užtenka turėti civilinės atsakomybės draudimą.

Taigi, nors pastarieji argumentai atrodo protingesni, praktika skiriasi. Tačiau dauguma teismų vis dėlto sutinka, kad subrogacijos klausimas turėtų būti sprendžiamas žiūrint į kiekvieną bylą atskirai ir laikantis teisingumo principų.