ANSWERS TO THE QUESTIONS

IN THE COURSE GUIDE

CPCU 552

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Assignment 1

Introduction to Commercial Liability Insurance

Educational Objective 1

A liability loss includes all costs to an organization because of a suit or claim made against it for damages or some other remedy permitted by law. If held legally liable, the organization must pay for the alleged injury. However, an organization can experience a loss even if it is not held legally liable (investigation and defense costs).

Legal liability, an enforceable obligation, can be imposed by civil, or criminal law, or both. Legal liability imposed by civil law can be based on torts, contracts, or statutes.

- A tort is a civil or private wrongful act or omission that invades legally protected rights of another. These rights include the right to personal safety, security of property, maintaining a good reputation, and the right to privacy. Torts can be classified as negligence, intentional torts, and strict liability.

(a) Negligence is an unintentional tort involving the failure of an individual to use reasonable care, (the care that a reasonably prudent person would have exercised under like circumstances), to avoid harming another. As a civil wrong leading to legal liability, the tort of negligence has four elements, all of which must be proven by the plaintiff in order to support the allegation. They are:

1. The defendant had a duty to the plaintiff to use reasonable care.
2. The defendant breached the legal duty.
3. The defendant’s negligent act or omission was the proximate cause of the plaintiff’s damages.
4. The plaintiff suffered an actual loss or damage.

(b) Intentional torts occur when a person foresees (or should have foreseen) that his or her action would harm another. The action does not have to be done with malicious intent. Libel is an intentional tort whereby the publication of a false statement harms another person’s reputation.

(c) Strict liability, also called absolute liability, is tort liability which may be imposed without proof of fault, i.e., without regard to negligence or intent to cause harm. Owning abnormally dangerous animals (wild lions), undertaking ultra-hazardous activities (blasting), and making defective products (medical drugs) are examples of liability being imposed if an injury is sustained by another because of these activities. Strict liability can also be imposed by certain statutes, such as workers’ compensation laws.

- Contracts, or legally enforceable agreements, can also impose liability. Each individual has certain duties under contracts, and legal liability arises out of the duty owed to another party. Liabilities based on contracts arise out of breach of contract or when one party has signed an agreement to assume the legal liability of another.

(a) Contract law governs breach of contract actions, which are suits brought by one party to a contract against the other. If one of the parties fails to honor the promise made, the other can sue in court to enforce the contract.

(b) Another exposure to legal liability based on contracts arises from assumptions of liability in contracts under which the assuming party agrees to bear the financial consequences of losses incurred by the other party. These contract provisions are usually called hold-harmless agreements or indemnity agreements. For example, in a lease, a tenant may agree to be responsible for any damage to the leased building, however caused.

Liability insurance policies generally do not cover breach of contract actions. Contractual liability insurance covers a limited set of prescribed assumptions of liability.

- A statute is a written law passed by a legislative body, at state or federal level. Legislatures can amend the common law or
create liability exposures which did not exist under common law. Statutes can modify the duties that persons owe one another which can lead to liability in tort action. They can also impose legal liability regardless of whether the person acted negligently, committed any tort, or assumed liability under a contract.

Statutes can impose a form of strict liability whereby an organization must compensate another if certain events occur. Such is the case with workers’ compensation laws. This type of legal obligation is based entirely on statute requirements rather than on tort law.

**Key Words and Phrases**

1. A **liability loss** is any loss that a person/organization sustains because of a claim or suit against it by someone seeking damages or other remedy.

2. Legal liability is the legally enforceable obligation of an organization or person to pay damages (money) to another person or organization.

3. Civil law – a classification of law that applies to matters not governed by criminal law that protects rights and provides remedies for breaches of duties owed to others.

4. Criminal law is the branch of law that imposes penalties for wrongs against society.

5. A **tort** is a wrongful act or omission, other than a crime or a breach of contract, which violates the legal rights of another.

6. Negligence is the failure to exercise the degree of care that would be exercised by a reasonably prudent person under similar circumstances in order to avoid hurting another.

7. Intentional torts occur when a person foresees (or should have foreseen) that his or her action would harm another.

8. Strict liability, or absolute liability, is liability imposed by a court or statute without regard to fault when harm results from activities/conditions that are extremely dangerous, unnatural, ultrahazardous, extraordinary, abnormal, or inappropriate.

9. A **contract** is a legally enforceable agreement, between two or more parties in which each make some promise to the other.

10. Breach of contract is the failure, without legal excuse, to fulfill a contractual promise.

11. A hold-harmless agreement, or indemnity agreement, is a contractual provision that obligates one party agrees to assume the legal liability of another.

12. **Contractual liability** is that liability assumed through a hold-harmless agreement.

13. A **statute** is a written law, enacted by a legislative body on either the state or federal level.

**Review Questions**

1-1. The costs that might result from a liability claim and covered under general liability policies would include all defense costs to investigate and defend the claim, and any resultant damages which would be awarded if the organization is found legally liable for the alleged injury.

1-2. A business can experience a liability loss even though it is found not to be legally liable for the loss, because the organization still has to pay for the costs to investigate and defend the claim.

1-3. The four elements of negligence liability are:

   (a) A legal duty owed. The defendant had a legal duty to the plaintiff to act with a certain degree of care.
   (b) Breach of the legal duty. The defendant failed to demonstrate a reasonable degree of care under the circumstances.
   (c) A causal connection. The defendant’s failure to use the degree of care that was owed resulted in harm to the plaintiff.
(d) Actual loss or damage. The damages of the plaintiff must be acknowledged as such by law and must be measurable in terms of monetary value.

1-4. (a) Intentional torts occur when a person foresees (or should have foreseen) that his or her action would harm another. The action does not have to be done with malicious intent. Libel (writing false statements which hurt the reputation of another) and slander (spoken false statements) are examples of intentional torts.

(b) Strict liability, or absolute liability, is liability which may be imposed by a court or statute without regard to fault and is not based on negligence or intent to harm. The nature of the activity itself, because it is extremely dangerous, unnatural, ultrahazardous, or abnormal, is the source of the liability. Owning a wild animal or engaging in blasting operations are examples of strict liability that may be imposed if harm results from these activities.

Statutes can also impose a form of strict liability whereby an organization must compensate another if certain events occur. Such is the case with workers’ compensation laws. This type of legal obligation is based entirely on statute requirements rather than on tort law.

1-5. (a) For instance – by law, any product for sale has an implied warranty that it is fit for the particular purpose for which it is sold. If a product is not suited for its intended purpose, and the buyer is injured as a result, the seller can be held legally liable for the damages under the concept of breach of contract (the implied warranty).

(b) For example, a contractor of a building can agree to hold one of his subcontractors harmless for work being done in the building. If because of negligence, the subcontractor is sued for harm to a third-party, the contractor would be responsible to pay for the claim made against the subcontractor because of the hold-harmless agreement.

**Application Question**

1-6. Agnes sells animals that are potentially dangerous in themselves, and therefore strict liability can be imposed even though she did not intend to harm and was not negligent in her buying or selling practices. Because the scorpion bit and injured a third-party, not only the owner who purchased the exotic pet from Agnes is liable, but the injured neighbor can seek redress from Agnes also.
MULTIPLE CHOICE

QUESTIONS WORKBOOK

Commercial Liability
Risk Management and Insurance

CPCU 552

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Assignment 1

Introduction to Commercial Liability Insurance

1. All of the following are ways in which a person or organization can become legally liable because of duties based or imposed by civil law, EXCEPT:
   - (A) Torts
   - (B) Statutes
   - (C) Allegations
   - (D) Contracts

2. A successful allegation of the tort of negligence is based on all the following elements, EXCEPT:
   - (A) A legal duty owed to another person
   - (B) A breach of that duty
   - (C) A close causal connection between the breach and the resulting harm
   - (D) An occurrence of loss or damage which cannot be measured in monetary terms

3. Joe’s Pizza rented a storefront in a building owned by Middletown Development Company. The lease for the property provided that Joe’s Pizza would hold harmless and indemnify the landlord against all liability arising out of the rental and use of the leased premises only.

   1. A tenant on his way to pay rent was injured when he slipped on the ice in front of the entrance to the landlord’s office located inside the building where Joe has his pizzeria. The man sued Middletown Development Company for bodily injuries.
   2. A fire occurred in one of the ovens while making pizza and caused damage to the inside of Joe’s leased areas of the building.
   3. Another fire from the pizza ovens caused damage to the entire building.
   4. A sewer main break in the street flooded the first floor of the leased building. Both the landlord’s and Joe’s Pizza Shop sustained damages.

In which of the following situations would Joe’s Pizza be responsible for the loss?

   - (A) Losses number 1. and 2.
   - (B) Losses number 2. and 3.
   - (C) Losses number 1. and 3.
   - (D) Losses number 3. and 4.
4. In which of the following would a plaintiff be successful in sustaining a cause of action under strict liability?

   (Text 1.5-1.6)
   
   (A) A family does not have a license for its German shepherd. The dog bites a neighbor.
   (B) Pets ‘R Us has cages containing exotic snakes. A customer is bitten when she puts her finger into the cage where the snake seemed to be sleeping.
   (C) A building collapsed two days after the contractor had completed the job. Three people were seriously injured.
   (D) All of the above.

5. Which of the following is an example of legal liability imposed by a state or federal law?

   (Text 1.6)
   
   (A) Failure to fulfill a contractual promise
   (B) Failure to provide benefits to an injured employee
   (C) Failure to exercise reasonable degree of care to another
   (D) Failure to protect others from an abnormally dangerous animal

6. All of the following are examples of a premises and operations liability loss exposure, EXCEPT:

   (Text 1.7-1.8)
   
   (A) A customer was injured three months after the contractor installed a new boiler in her home when the boiler exploded.
   (B) An organization’s bulldozer accidentally damages a building next to its worksite.
   (C) A retail company is sued when a customer fell on the ice outside the company’s front door.
   (D) A blasting contractor unintentionally blows out windows in buildings near its blasting operations.

Assignment 1

Introduction to Commercial Liability Insurance

1. C is the answer. Legal liability imposed by civil law can be based on torts, contracts, or statutes. Allegations can be true or false. However, even if the allegation is proven false and there is no legal liability implied, the CGL insurer must still pay for the defense costs of its insured.

2. D is the answer. The four elements needed for a successful allegation of negligence are A, B, C, and an occurrence of actual loss or damage of a type recognized by law and measurable in monetary terms.

3. B is the answer. Joe’s Pizza is only responsible for damage resulting from his operations within the leased building. Since both fires originated inside his leased portion of the building, Joe’s is responsible for the damage not only to his leased premises but for the damage to the rest of the building also. The hold-harmless agreement did not obligate Joe’s to indemnify Middletown for any person injured on the leased premises (1.) and Joe’s is certainly not responsible for the sewer leak (4.).

4. B is the answer. Strict liability is imposed even though the defendant acted neither negligently nor with intent to cause harm. Snakes are considered inherently or abnormally dangerous and so the plaintiff would be successful in bringing a cause of action under strict liability. A dog biting a neighbor and a building collapsing do not come under the definition of strict liability.

5. B is the answer. An employer’s responsibility to pay claims under workers’ compensation statutes is liability imposed by law. In addition to torts and contracts, statutes are a third major basis for imposing legal liability.
6. A is the answer. Under the example in A, this is a completed operations liability loss exposure. Premises and operations liability loss exposures relate to liability arising from injury or damage that occur on an organization’s owned, leased, or rented property, or by an accident arising out of its ongoing operations away from its premises. B, C, and D are examples of this.