Lesson 1 Essentials of Legal Liability

Introduction

In the three policies we will cover later in this course, the greatest majority of coverage arises from an insured person's legal liability. Legal liability is a responsibility or obligation to others, which the courts recognize and enforce. Legal liability is the event that triggers (initiates) coverage in most of the policies we will discuss.

Legal liability can come from many exposures. There are also several types of legal liability that an insured person can be exposed to. In addition, different types of damages (amounts of money) may be assessed when legal liability occurs.

In this lesson we will focus on liability exposures. It is important to learn what they are, before learning if and how they are covered by an insurance policy.

**Exposure**: Units used to measure loss costs. Typically payroll is used for workers compensation, number of vehicles for auto liability, revenue for general liability and number of units in service for products liability. Forecasts of exposures can be used to forecast future losses. The state of being subject to loss because of some hazard or contingency. A situation, practice or condition which might lead to a loss; an activity or resource (assets, people).

Some exposures are covered by the CGL Policy and some are not. As you go through the lessons, make sure you remind yourself about the difference between "exposures" and "coverages."

In lessons 2 through 6, we will study how the Commercial General Liability (CGL) Policy, the Business Auto Policy (BAP), and the Workers Compensation (WC) Policy provide coverage for many of the exposures we are about to study.

This lesson will consist of four topics:

1. Types of Liability
2. Direct and Vicarious Liability
3. Types of Damages
4. Liability Exposures
Learning Objectives

After completing this lesson, you will be able to:

1. Define three categories of legal liability: tort, statutory and contractual.
2. Explain four types of tort liability and give an example of each.
3. Name the four requirements of a negligent tort.
4. Explain the concept of direct liability.
5. Define vicarious liability, and give examples of relationships where vicarious liability may be created.
6. Name and describe the types of damages that may be awarded in a civil court case.
7. Identify and explain the sources of legal liability exposures.

Forms Used In This Lesson:
None
Lesson 1 Topic A - Types of Liability

Learning Objective: Define three categories of legal liability: tort, statutory and contractual.

Legal liability is "a responsibility or obligation to others, which courts recognize and enforce." In general, failure to meet this duty often results in the imposition of monetary damages.

The three types of legal liability that we will cover in this lesson are:

- Tort Liability
- Statutory Liability
- Contractual Liability

Learning Objective: Explain four types of tort liability and give an example of each.

Tort Liability

The Commercial General Liability Policy and the Business Auto Policy both refer to tort liability. A basic definition of tort is a civil legal wrong against another for which the courts often assess monetary damages against the wrongdoer. Tort liability is imposed by common law, that is, law that has been developed through the application of court case decisions over time. You will need to be familiar with four types of torts:

1. Negligence
2. Intentional Torts
3. Strict Liability
4. Absolute Liability

We will go into more detail of the four types of tort liability on the pages that follow.
Learning Objective: Name the four requirements of a negligent tort.

- **Negligence**

A basic definition of negligence is the failure to act as a reasonable person would under the same or similar circumstances. Failure to do so can result in a negligent tort. You need to remember that four elements or components are required for a negligent tort:

1. There must be a **duty owed** by the negligent party to another party. A person has a duty to operate an automobile safely
2. There must be a **breach of that duty**. The person runs a red light
3. An actual **injury or loss must occur**. Their action caused a collision
4. There has to be a close cause and effect (proximate cause) relationship between the breach of that duty and the injury or loss. The result was property damage to the other car and bodily injury to the other driver
Learning Objective: Explain four types of tort liability and give an example of each.

2. **Intentional Tort**

   An intentional or voluntary act can result in injury or loss to another party, and the person committing the act can be held legally liable for that injury or loss. Examples include:
   
   1. Libel
   2. Slander
   3. Wrongful entry or wrongful eviction
   4. Assault and/or battery
   5. Wrongful detention
   6. False arrest
   7. Copyright infringement, trademark infringement, etc.

3. **Strict Liability**

   Strict liability is a concept applied by the courts in product liability suits in which a manufacturer, distributor, or seller is liable for any and all defective or hazardous products that unduly threaten a consumer’s health and safety. Unlike the case of negligence previously discussed, the element or component of proximate cause is not applied. All that has to be proved is that a product injured someone or caused damage.

   **Examples of strict liability losses include:**
   
   - A football player was injured while wearing a football helmet. The helmet was not defective and was being used properly. The fact that the helmet did not do what it was intended to do (protect from head injury) was cause for strict liability.
   
   - A 300 pound man was injured when a ladder he was using collapsed. The ladder was rated for maximum capacity of 250 pounds. The court found contributory negligence on the part of the injured man. However, the manufacturer was still held partially liable for the injury.
Learning Objective: Explain four types of tort liability and give an example of each.

4. Absolute Liability

Absolute liability, like strict liability, is also considered liability without fault or negligence. Absolute liability applies when conditions or activities are dangerous by their very nature and are allowed to exist, even when the insured has taken every precaution to prevent or reduce any type of loss. All that has to be proved is that an injury or damages occurs because of the conditions or activities.

Examples of absolute liability include:

- Explosive or blasting operations
- Dangerous animals
- Hazardous material operations
Learning Objective: Explain four types of tort liability and give an example of each.

### Review Our Study

#### Torts

**Negligence**
Example: If a driver runs a stop sign, the driver breached a duty owed. But unless they cause injury or property damage, there is no negligent tort.

**Intentional Acts**
Examples include:
- Libel
- Slander
- Wrongful entry or wrongful eviction
- Wrongful detention
- False arrest
- Copyright infringement, Trademark infringement

#### Statutes

**Strict Liability**
Example: Product liability - A container advertised to hold toxic chemicals leaks when the consumer puts the chemical in the container

**Absolute Liability**
Examples:
- Explosive or blasting operations
- Dangerous animals (whether known to be dangerous or not)
- Hazardous material operations

#### Contracts

Types of Tort Liability

- Negligence
- Intentional acts
- Strict liability
- Absolute liability
Knowledge Check

Match each type of tort on the left with the corresponding example on the right.

<table>
<thead>
<tr>
<th>Type of Tort</th>
<th>Example</th>
</tr>
</thead>
<tbody>
<tr>
<td>Absolute Liability</td>
<td>A neighbor’s child is injured by a pet lion.</td>
</tr>
<tr>
<td>Negligence</td>
<td>A toaster does not shut off and starts a fire in the kitchen.</td>
</tr>
<tr>
<td>Intentional Act</td>
<td>A teenager deliberately throws a rock at a glass window and breaks it.</td>
</tr>
<tr>
<td>Strict Liability</td>
<td>A driver runs a red light and causes vehicle damage to another vehicle</td>
</tr>
<tr>
<td></td>
<td>in an auto accident.</td>
</tr>
</tbody>
</table>

The correct answers are below:

**Absolute Liability:** A neighbor’s child is injured by a pet lion.

**Negligence:** A driver runs a red light and causes vehicle damage to another vehicle in an auto accident

**Intentional Act:** A teenager deliberately throws a rock at a glass window and breaks it.

**Strict Liability:** A toaster does not shut off and starts a fire in the kitchen.
Learning Objective: Define three categories of legal liability: tort, statutory and contractual.

Statutory Liability

Statutory liability is liability arising out of specific rules or laws (statutes) enacted by a legislative body providing direction or prohibition. The existence of these statutes subjects a business owner to liabilities imposed by the provisions of the laws. Statutes over-ride common law.

Examples of Statutory Liability

- Workers Compensation Laws
- Dram Shop or Liquor Liability Laws
- Environmental Protection Laws
- Americans With Disabilities Act, related rulings and state laws
- Employment Liability through laws and EEOC rulings
Learning Objective: Define three categories of legal liability: tort, statutory and contractual.

Contractual Liability

A contract is an agreement between two or more parties, which creates an obligation to do or not to do a particular thing. Often in contracts, one party assumes the financial consequences of certain liabilities of another.

Contractual liability includes:
- Assumption of liability
- Breach of contract

Parties commonly involved:
1. Lessor-Lessee
2. Owner-Contractor
3. Contractor-Sub Contractor
4. Manufacturer-Distributor

Later in this course, we will see that not all contractual assumptions of liability will be covered by insurance policies. The policies will grant coverage for "insured contracts" only.
Learning Objective: Define three categories of legal liability: tort, statutory and contractual.

Contractual Liability Examples
When a tenant signs a lease, he or she may agree to pay for any judgment assessed against the landlord because of activities at the rented premises.

Another common example can be found in an equipment lease. When you sign a lease for a phone system or computer equipment, you agree to assume the costs of any judgment assessed against the owner of the equipment for losses occurring while you have the equipment. This is a common contractual assumption of the liability of another.

Parties may be liable for breach of contract. However, breach of contract will not be covered by most liability policies.

Not all contracts are "insured contracts!" Insured contracts will be defined in Lesson 3 Topic B.
Tort

- **Negligence**: There are four requirements of a negligent tort. There must be:
  1. A duty owed
  2. A breach of duty
  3. Proximate cause
  4. Damages

- **Intentional Torts**: Examples of intentional torts include: libel, slander, wrongful entry or wrongful eviction, assault and/or battery, wrongful detention, false arrest, and copyright infringement and trademark infringement.

- **Strict Liability**: For strict liability, all that has to be proved is that a product injured someone or caused some damage.

- **Absolute Liability**: Examples of absolute liability include: Explosive or blasting operations, dangerous animals, and hazardous material operations.

Statutory

- **Imposed by Laws and Regulations**: Examples: Workers Compensation Laws and Americans with Disability Acts-related rulings and statute laws.

Contractual

- **Assumption of Liability**: Example: A common contractual assumption of the liability of another would be renting equipment and the contract states you agree to assume the costs of any judgment assessed against the owner of the equipment for losses occurring while you have the equipment.

- **Breach of Contract**: Insurance policies will grant coverage for "insured contracts" only and not cover all contractual assumptions of liability.

  Note: Not all contracts are "insured contracts." Parties may be liable for breach of a contract; however, a breach of contract will not be covered by almost all liability policies.
Lesson 1 Topic B - Direct and Vicarious Liability

The majority of liability claims involve the tort liability of your client. In general, tort liability can be triggered from two types of actions. They are:

1. **Direct Liability**: Results from your client's conduct

2. **Vicarious Liability**: Results from the conduct of others

**Learning Objective**: Explain the concept of direct liability.

**Direct Liability**

Direct liability results from the conduct of a business that is responsible for injury or property damage to another.

**Example**

- Deem's Market, Inc. fails to clean up a food spill in one of its grocery aisles, and a patron slips on the food, falls and breaks several bones. The claimant sues Deem's Market, Inc. because it directly caused the injury.

**Learning Objective**: Define vicarious liability, and give examples of relationships where vicarious liability may be created.

**Vicarious Liability**

Vicarious liability is the liability of one party based upon the liability of another. It is said that liability is imputed (transferred from one party to the other).

Many times the named insured is not actively involved in the conduct that causes injury or damage, and in fact may have actually discouraged it or tried to prevent it. However, because of the nature of certain relationships, the conduct of others can create vicarious liability for the named insured.

**Example**

- While delivering groceries, an employee of Deem's Market, Inc. causes an auto accident in which three people are injured. The injured parties bring a claim against the employee who directly caused the accident, but they also bring a claim against Deem's Market, Inc., because Deem's Market, Inc. can be held
vicariously liable for the actions of its employees done within the scope of employment.

Learning Objective: Define vicarious liability, and give examples of relationships where vicarious liability may be created.

<table>
<thead>
<tr>
<th>Relationship</th>
<th>Example</th>
</tr>
</thead>
<tbody>
<tr>
<td>Employer/Employee</td>
<td>Legal doctrine has held that the employer is responsible for injury or damage to another, resulting from the acts of an employee done within the scope of the employee's employment while in the employer's service. The employee can be held individually liable for their acts. However, in the real world it is the employer, more times than not, who has assets and who will bear the financial burden of the employee's acts.</td>
</tr>
<tr>
<td>Principal/Agent</td>
<td>This is similar to the employer/employee relationship. However, the principal is liable only for acts of the agent while the agent is performing acts directly related to the relationship. A real estate company could be legally liable for acts or omissions of its independent realtors while acting on behalf of the company.</td>
</tr>
<tr>
<td>Owner/Manager</td>
<td>A property owner could be legally liable for the acts or omissions of its management company. Like the principal/agent relationship, the owner can be liable only for acts performed by the manager directly related to the relationship.</td>
</tr>
<tr>
<td>Owner/Contractor/Subcontractor</td>
<td>An owner/contractor may be held liable for the acts of its contractor/subcontractor. However, generally the owner/contractor is not held legally liable for the conduct of a subcontractor unless the subcontractor is performing inherently dangerous acts or the owner/contractor was negligent in choosing them. This is not as automatic as the employer/employee relationship.</td>
</tr>
</tbody>
</table>

Please refer to the end of Lesson1 Topic B to complete Self Quiz 1.
Learning Objective: Name and describe the types of damages that may be awarded in a civil court case.

In liability, we refer to the money awarded in a suit or claim as damages. There are two basic types of damages that are awarded in liability claims. They are:

- Compensatory damages
- Punitive or exemplary damages

Compensatory Damages

Compensatory damages are sums of money that will, as far as possible, compensate for the loss. There are two types of compensatory damages:

1. **Special Damages:** Specific dollar amounts that cover specific costs.
   - **Examples:**
     - Medical bills, lost income, rehabilitation expenses, repair or replacement of property, loss of use of property, etc.

2. **General Damages:** Subjective dollar amounts that cover intangible losses.
   - **Examples:**
     - Pain and suffering, loss of consortium, etc.

Punitive or Exemplary Damages

Punitive or exemplary damages are sums of money, more than that required to compensate for loss, which are imposed in order to punish wrongdoer conduct now and deter such conduct in the future.

Statutes may restrict the amount of exemplary or punitive damages that can be recovered. State law may also restrict liability policies from paying for exemplary or punitive damages. In addition, some liability policies have exclusions that prohibit paying for exemplary or punitive types of damages.

Judge: “I am going to **punish** the wrongdoer for his conduct and this will deter such conduct in the future!”
Knowledge Check

Drag and drop each number into the corresponding damages bucket.

1. Compensation in excess of actual damages
2. Pain & suffering
3. Lost income
4. Compensation for malicious conduct
5. Punishes the defendant
6. Medical bills
7. Repair or replacement of property

The correct answers are below.

**Compensatory Damages**
- Medical bills
- Lost income
- Pain & suffering
- Repair or replacement of property

**Punitive Damages**
- Compensation in excess of actual damages
- Compensation for malicious conduct
- Punishes the defendant
Lesson 1 Topic D - Legal Liability Exposures

Learning Objective: Identify and explain the sources of legal liability exposures.

Our commercial insureds face various types of risks every day. Business entities - whether individuals, partnerships, or corporations, are subject to many exposures that can create legal liability. The owners or individuals responsible for the operation of the business do not always recognize every exposure. You can help your client to identify some of these exposures.

Common business exposures that can lead to legal liability are:

- Premises
- Operations
- Products
- Completed Operations
- Ownership, Maintenance, or Use of Autos
- Ownership, Maintenance, or Use of Other Conveyances
- Employing Workers
- Liquor
- Environmental Impairment
- Professional Activities
- Bailee Liability

Premises Liability

Legal liability results out of an injury and/or damage due to the ownership, maintenance, or use of a location. The exposure applies to owners, landlords, and tenants, and is generally confined to a specific location(s), like the address of the business.

Examples

- A customer slips and falls in a store due to water on the floor.
- A fire accidentally started by an employee damages property belonging to the business next door.
Learning Objective: Identify and explain the sources of legal liability exposures.

Liability Arising from Operations

Legal liability results when injury and/or damages arises out of business activities (such as construction, processing, manufacturing, repairing, or loading and unloading goods, etc) which are necessary and incidental for conducting business. The exposure can be at the premises or at other locations where the business activity occurs.

Examples
- A tree-removal contractor causes damage to power lines when removing tree limbs.
- During the loading process, a load of boxes falls off a conveyer belt injuring a customer.

Products Liability

Legal liability results when injury and/or damage arises out of defects in product design, manufacture, or the failure to warn or explain.

The exposure applies to the use of a product made or sold by the business. This exposure begins after the sale and as soon as the product has left the premises.

Examples
- A table collapses because improperly sized screws were used in construction, causing damage to a customer's computer.
- A manufacturer fails to warn of choking danger associated with small parts on a toy, and a child chokes on a part when given the toy.
Learning Objective: Identify and explain the sources of legal liability exposures.

Liability Arising from Completed Operations

Legal liability results when injury and/or damage arises out of defective or improper workmanship. The exposure applies to the insured's work. This exposure begins once the operations have been completed and the insured leaves the work site.

Examples
- Several weeks after an electrician uses the wrong size wire for a repair, a resulting fire damages the customer's building.
- An employee improperly installs a hot water heater. Three days later the building is flooded with gallons of water.

Liability due to the Ownership, Maintenance, or Use of Automobiles

Legal liability results when injury and/or damage arises out of the ownership, maintenance, or use of an auto, including entrustment and/or supervision. Almost every commercial client has this exposure.

Examples
- While making deliveries in a company auto, an employee runs a red light and causes an accident.
- A poor maintenance program causes the improper braking ability of a company vehicle, which results in an accident.

Liability due to the Ownership, Maintenance, or Use of Other Conveyances

Legal liability results when injury and/or damage arises out of the ownership, operation, maintenance, or use of conveyances other than an auto. The exposure will vary from business to business.

Examples
- Injury or damage is caused by use of mobile equipment such as a forklift.
- The use of watercraft, aircraft, or recreational vehicles causes harm or injury.
Learning Objective: Identify and explain the sources of legal liability exposures.

Liability due to Employing Workers

Legal liability arises from the statutory obligations employers have to employees regarding work-related injuries or occupational disease. This liability may also cover various consequential injuries to others, caused by the employee’s injury or disease. The exposure is subject to the laws and regulations governing Workers Compensation, Employers Liability Coverage, and other employment related issues in each state.

Examples

- An employee ruptures a disc while lifting a box of paper.
- An employee develops chemical pneumonia from inhaling acidic fumes while cleaning machinery.

Liquor Liability

Legal liability is imposed in most states when injury and/or damage arises from the business of manufacturing, distributing, selling, serving, or furnishing of alcoholic beverages. The exposure will vary and is subject to statutes and case law in each state.

Examples

- An employee becomes intoxicated at a company-sponsored picnic, where the company provided alcoholic beverages, and injures someone while driving home.
- A bar customer becomes intoxicated after consuming alcoholic beverages and injures someone while driving home.
Learning Objective: Identify and explain the sources of legal liability exposures.

Liability Arising from Environmental Impairment
Legal liability may be imposed by statute or because of injury and/or damage. The exposure may arise from direct or indirect involvement with pollution and/or pollution-related situations.

Examples
- Your negligent operation of a vehicle results in an accident, causing hazardous chemicals to leak from the other vehicle, gasoline to leak from the gas tank of your vehicle, and your cargo of toxic waste to be spilled.
- Your own commercial property contains leaking underground chemical tanks or lead-based paint.

Liability Arising from Professional Activities
Legal liability results from injury and/or damage arising from the giving or failure to give professional advice or service. The exposure will vary depending on the nature of the business and by state statute and case law.

Examples
- A CPA gives the wrong advice, resulting in IRS penalties and/or fines.
- An architect makes a design mistake, causing a load-bearing wall to collapse.

Bailee Liability
Legal liability results from injury and/or damage arising out of the insured's possession of other's property. The exposure will vary on the nature of the business.
Summary

The next two pages list some sources of exposures. They are not all-inclusive. However, they do include the majority of sources that businesses encounter that can result in legal liability.

Common Business Liability Exposures

- **Premises**: Legal liability results out of an injury and/or damage due to the ownership, maintenance, or use of a location.

- **Operations**: Legal liability results when injury and/or damages arises out of business activities such as construction, processing, manufacturing, repairing, or loading and unloading of goods.

- **Products**: Legal liability results when injury and/or damage arises out of defects in product design, manufacture, or the failure to warn or explain. The exposure begins as soon as the product has left the premises.

- **Completed Operations**: Legal liability results when injury and/or damage arises out of defective or improper workmanship. The exposure applies to the insured's work. The exposure begins once the operations have been completed and the insured leaves the work site.

- **Ownership, Maintenance, or Use of Automobiles**: Legal liability results when injury and/or damage arises out of the ownership, maintenance, or use of an auto. Almost every commercial client has this exposure.

- **Ownership, Maintenance, or Use of Other Conveyances**: Legal liability results when injury and/or damage arises out of the ownership, operation, maintenance, or use of conveyances other than an auto. This exposure will vary from business to business.

- **Employing Workers**: Legal liability arises from the statutory obligations employers have to employees regarding work-related injuries or occupational disease. The exposure is subject to the laws and regulations governing Workers Compensation, Employers Liability Coverage, and other employment related issues in each state.

- **Liquor**: Legal liability is imposed when injury and/or damage arises from the business of manufacturing, distributing, selling, serving, or furnishing of alcoholic beverages. The exposure will vary and is subject to statutes and case law in each state.
• **Environmental Impairment:** Legal liability exposure that may arise from direct or indirect involvement with pollution and/or pollution-related situations.

• **Professional Activities:** Legal liability results from injury and/or damage arising from the giving or failure to give professional advice or service. The exposure will vary depending on the nature of the business and by state statute and case law.

• **Bailee:** Legal liability results from injury and/or damage arising out of the insured's possession of other's property. The exposure will vary on the nature of the business.

Please refer to the end of Lesson1 Topic D to complete Self Quiz 2.