Insurance Alert

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New Developments in CGL Policy Wording

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In December 2001, the Insurance Services Office (ISO) implemented significant changes in the Commercial General Liability (CGL) policy form. The purpose of this article is to provide both an overview of some of the major changes and to foster basic awareness that can be used in later discussions with your carrier, broker, risk manager or other insurance professional.

Who is an Insured?

The “Who is an Insured” section of the CGL policy includes several new features:

a) “volunteers” are being added as automatic additional insureds, so organizations which now use volunteer workers on a regular basis will have expanded coverage.

b) trusts can now be included as named insureds, if listed, with automatic coverage also provided for trustees.

c) a new standard ISO endorsement has been developed to afford completed operations coverage for additional insureds.

The last change is most significant, as coverage for this particular exposure had been difficult to get in the past. In the course of its usual business operations, an insured may negotiate contracts requiring it, among other things, to add a third party to its policy as an additional insured. For example, contractors or suppliers doing business with government organizations are frequently required to name a particular state or local agency as an added insured. Failure to comply with a contractual obligation to provide another entity with additional insured status can result in a breach of contract claim against the insured. Problems could arise, however, where the insured’s contractual requirements included affording completed operation coverage to the added third party. In the past, no standard endorsement existed and underwriters were reluctant to provide the coverage. With the introduction of ISO’s new endorsement extending completed operations to additional insureds, the vehicle for addressing this exposure exists - but it must be negotiated on a case by case basis. Therefore, speak to your broker or carrier if attachment of this endorsement will benefit your insurance program.

Loss or Damage

Unknown Prior to Policy Period

Insurance companies prefer not to underwrite burning buildings as risks - it's just not good business! A basic principle of liability insurance is
that it responds only to unknown losses. While the principle appears self-evident, it wasn’t until recently that the CGL form actually focused on it within the policy language. In Montrose Chemical Corporation v. Admiral Insurance Company, 913 P.2d 878 (Cal. 1995), the California Supreme Court ruled that while the insured knew of a loss prior to policy inception, the insurer was nevertheless still required to provide coverage until the insured’s legal obligation to pay third party claims was established. As a result of this decision, ISO introduced a rider in 1999 stating that the CGL applied only to unknown losses. The 2001 policy revisions now incorporates explicit language directly into the form itself stating that coverage only applies to loss or damage unknown prior to the policy period.

Coverage for Computer Data

In a previous Insurance Alert, we addressed the judicial debate about the application of standard insurance policies to data and computers (“Courts Disagree on Insurance Coverage for Data,” October 2001). The insurance industry wants to short-circuit this debate and, consequently, ISO has redefined the term “Property Damage” to specifically state that electronically stored data or software is not tangible property “for the purposes of this insurance,” thereby removing potential coverage for damage to data or software and loss of use resulting from that damage. Thus, someone with a standard CGL form who becomes legally liable for a customer’s lost electronic data within its computer system will be out of luck as respects coverage.

However, an absolutely impenetrable coverage gap is not created by the exclusion of data/software from the definition of property damage. ISO is stepping into the void resulting from this change and will introduce two new coverage options to meet policyholder needs. The first is an electronic data liability endorsement (filed for availability in the first half of 2002) that will provide coverage for loss of data resulting from physical injury to tangible property. Later in 2002, ISO expects to introduce an even broader electronic data liability coverage form that will provide for actual damage to the electronic data itself. If required, insureds should consult their brokers about the availability of these options.

Internet Liability

The uninterrupted growth of the Internet as a medium for delivering goods and services continues to impact legal liability. insurers have recently introduced various products addressing e-risks, such as cyber-terrorism, identity theft, hackers, etc. However, to facilitate increased demand for these new specialty policies, the insurance industry has simultaneously added new exclusions to the CGL, in order to prevent any coverage overlap.

With respect to Personal and Advertising Injury coverage, ISO has added web site creators and internet access providers to the list of those excluded from coverage (that group previously including advertisers, broadcasters, publishers and telecasters). A new exclusion has been added for those hosting bulletin boards and chat rooms, since some courts have determined that these businesses
are also publishers. In addition, a personal and advertising injury exclusion has been added to preclude coverage for companies that employ tactics to mislead and divert Internet customers by the unauthorized use of another’s name or product in a domain name, e-mail address or metatag. At the end of the day, ISO’s bottom-line goal is to continue introducing cutting edge, niche products that respond to cyber-torts, while keeping the CGL out of play on those same issues.

On the positive side, ISO has clarified the personal and advertising injury definition to apply to defamation, disparagement or violation of privacy “in any form,” thus embracing all electronic media. The definition of “advertisement” has undergone revision, to include notices published or posted via the Internet. Lastly, coverage territory has been redefined to include offenses that take place through the Internet or other means of e-communication.

Changes to “Your Work” Exclusion - Removal of Exception for Subcontractors

The CGL form excludes property damage to the named insured’s work if the damage arises out of the insured’s workmanship and is included within the products-completed operations hazard. However, this exclusion often contains an exception for subcontractors, whereby it does not apply to damage to work performed by a subcontractor on behalf of the insured.

Continued recent development in the residential and commercial real estate markets has resulted in an increase of claims relating to construction defects. The insurance industry views this as a progressively difficult problem: when subcontractors are used extensively on a project, the risk of construction defects increases exponentially, as does the likelihood of claims made against the insured’s CGL.

To counteract those risks, ISO has made available two new optional endorsements that now restrict coverage by deleting the exception for subcontracted work. One removes the exception for all subcontracted work, while the other applies to selected operations only.

Both insureds (especially general contractors) and their sub-contractors need to be attentive to this change. The sub-contractor who relies on this exception for coverage must check with the insured if in fact its policy still contains the exception. If the named insured agreed, as part of the contract with its subcontractors, to secure coverage on their behalf, it must be certain that its CGL policy wasn’t renewed with these restrictive endorsements attached - or else face the possibility of being stuck with both the liability of, and a breach of contract claim from, the subcontractor.

Amendment to the “Owned Property” Exclusion

New language has been added to Exclusion j., Damage to Property, based on case law that opened the door to coverage for repairs made to an insured’s property, where such repairs are undertaken based on a duty to prevent additional injury or damage to a third party property. In Aetna Insurance Company v. Aaron, 685 A.2d 858 (Md.
App. 1996), the insured owned a condominium unit that included a large glass enclosure. The owner of the unit below the insured began to experience water leaks in her home as a result of structural problems inherent in the insured’s glass enclosure. The problem was fixed at a cost of almost $100,000, but when the insured submitted the claim to the insurer, the insurer denied coverage on the grounds of the owned property exclusion. The insured brought a declaratory action seeking coverage and the court agreed that coverage was merited. The court held that the owned property exclusion did not bar coverage of a claim for repairs to the insured’s own property, where the insured’s property first caused damage to a third party’s property and the insured had a duty to remediate in order to prevent imminent, additional damage to the other’s property. See id. at 872. Now, as a result of its changes to the exclusion, ISO has further restricted coverage by explicitly ruling out protection for those kinds of repairs dealt with in Aaron.

Revision to Exclusion G. - Negligent Supervision Not Covered

A standard exclusion in the CGL form applies to bodily injury or property damage arising out of the ownership, maintenance, use or entrustment to others of any aircraft, auto or watercraft owned or operated by the Insured. In practical terms, the industry intends for this kind of risk to be picked up via a separately purchased automobile policy.

Notwithstanding, a recent court case found coverage under CGL for injuries arising from an automobile accident, where the driver was operating a vehicle in the course of his employment. Although the injuries occurred in an auto accident, the plaintiff argued that the injuries arose from the employer’s negligent supervision of the its employee, the driver, and not from ownership or use of an auto as required by the CGL exclusion. The court agreed and ruled that negligent supervision is not clearly and unambiguously excluded from coverage. Thomas Milfred Pablo v. Scott Allen Moore, 995 P.2d 460 (Mont. 2000).

As a result of the uncertainty engendered by this decision and others like it, ISO has revised Exclusion g. by adding a paragraph clarifying that the exclusion applies even where there is an allegation of negligence or other wrongdoing in the supervision, hiring, employment, training or monitoring of others by the insured.

Availability of Employee Benefits Liability Coverage

For the first time, ISO is introducing its own employee benefits liability (EBL) endorsement. Until now, carriers offering this coverage did so via independent manuscript forms. This new endorsement will attach to the CGL and will cover obligations to pay damages and defense costs because of negligent acts, errors or omissions committed in the administration of an employee benefits program. Those with businesses that provide employee benefits, but who do not have insurance for damage due to negligent administration of those benefits, should consider this new EBL coverage.
It is worthwhile to note that unlike most CGL coverage, which is underwritten on an occurrence basis (e.g., coverage is available for loss events that occur during the policy period, regardless of when the claim is actually made), ISO’s new EBL coverage is offered on a claims-made basis; thus, coverage is available only in the event a claim is first made and reported to the insurer during the policy period. Insureds opting to attach the EBL endorsement to their CGL policy must remain aware of this crucial distinction because, as with any claims-made coverage, the timeliness and specificity of the claim notification is a condition precedent to obtaining coverage.

**Conclusion**

This alert is meant as a general overview, not as an all-inclusive exposition. Several other revisions now being made to the CGL are not addressed herein due to space constraints (including personal injury coverage for lawyers acting outside the legal profession, limited product withdrawal coverage (first party), and endorsements granting worldwide coverage). If you need additional information or advice, the Insurance Practice Group at Lowenstein Sandler remains available to discuss any coverage related issue with you and act as your resource in navigating the tricky pathways of insurance policy wording.

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