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1 Basics of Property & Casualty Insurance

Purpose of Insurance

The purpose of insurance is to spread risk amongst others and is intended to provide a practical solution to economic uncertainties and unexpected losses.

Types of Risks (uncertainty of loss)

1. Speculative Risk: This risk implies that an individual could not only have the potential of improving his/her financial position but also has the potential to being placed in a worse financial position by losing something. The best example for speculative risk is GAMBLING. Therefore, insurance policies will NOT protect speculative risks.

2. Pure Risk: On the other hand, this risk is what insurance is all about. It covers losses only and does not imply that the insured can “make money” after a covered loss. The goal of insurance is to place the insured back to his/her financial position just prior to the loss. Obviously, life insurance can’t replace the deceased, but instead, will help provide financial stability to the family or loved ones of the deceased.

What Produces Risks?

1. Hazards: These are things that might cause a peril, which creates the risk, which leads to a loss. As an example, an individual has heart disease (hazard) which causes a heart attack and the person dies.

2. Perils: A peril is the immediate, specific cause of a loss. Using the above example, the hazard (heart disease) gave rise to the potential cause of death, which is the heart attack, (known as a peril) that eventually causes the actual loss (death), and therefore creates a claim on the life insurance policy.

- Policy Perils

  - Property and casualty insurance policies are written in one of two ways concerning the perils covered. The first are named perils and the second type known as all risk or open perils.

  - Named perils lists the specific perils that it will cover. Obviously, in order for the insured to collect, the spe-
specific loss must be covered or the insured will not recover.

◊ On the other hand, an all risk or open perils policy covers all risk of loss or all perils except those that are specifically excluded.

**Loss**

Loss is an unintended or unforeseen reduction or destruction of financial or economic value. If an insured’s building burned to the ground, this event would be considered a total loss because the value of the ashes would be drastically different than the value of the home before the loss.

- **Direct Loss** is a loss, which occurs directly through an “unbroken chain of events” as a result of an insured peril. This is done without any intervening cause.

- **Indirect or consequential loss** is a loss or damage, which results from a hazard or peril, but the loss was not actually caused by that hazard or peril. These are losses, which result from the actual physical loss itself.

  ◊ Example: a fire burns a clothing store to the ground. The direct loss from the fire peril would be the total destruction to the building and its contents. The indirect loss from the fire peril would be the inability of the clothing storeowner to conduct business following the fire loss.

**Examples of Hazards**

- Employee hates his employer and “wants to get him.” *(Morale Hazard)* This is an attitude problem!

- An individual decides to burn down someone’s home. *(Moral Hazard)*

- **Physical Hazard** - These are physical, tangible items that can create a peril. Examples can include piles of oily rags, bad brakes, no brakes, slippery falls due to wax, skate board on the stairs etc.

**Accident vs. Occurrence**

Property and casualty contracts are usually written in two ways:
1. Accident-basis

An accident is a sudden unexpected, unforeseen event resulting in financial loss.

**Example:** Man falls on a cracked sidewalk. A truck hits a car. Lightening strikes a house causing a fire.

2. An Occurrence

An occurrence is a sudden, unexpected unforeseen event resulting in financial loss including repeated and continuous exposure to conditions.

**Example:** Industrial waste *gradually* pollutes a river. An insured worker *gradually* becomes ill due to repeatedly handling asbestos on the job.

Deductibles

In order to avoid minor claims, companies usually write deductibles into their property contracts. This means that the insured must pay some portion of the loss. Just like in health insurance, the insured will pay the deductible first and then the insurance company will pay the remainder of the claim within covered limitations.

Managing Risks

The following are ways that risks can be “managed”.

1. **Avoidance:** If you avoid doing something, like not driving an automobile, you will avoid the possibility of a loss involving an automobile.

2. **Assumption:** Instead of purchasing insurance you decide to assume the risk by self-insuring. An example of this would be declining fire insurance for your home. If the house burns down, you will not be reimbursed for the loss as you assumed it.

3. **Transfer:** This choice is what insurance is all about and is the most common way to manage risks. Transfer the risk to the insurance company and have the insurance company pay for any losses.

4. **Sharing:** While you transfer most of the risk to an insurance company you may have to share part of the losses. Examples of this
would exist in health, auto and casualty insurance through the use of deductibles and co-insurance requirements.

5. Reduction: Examples of risk reduction is the installation of smoke detectors, sprinkler systems, burglar and fire alarm systems and the use of air bags in autos. Some insurance companies offer special rate reductions when you have some of these.

Rules:

1. Law of Large Numbers: Actuaries look at similar type losses using large numbers of incidents. The word Homogeneous defines this process. With a large enough pool of risks, an insurer can predict with reasonable accuracy the number of claims it will have during any given time.

2. The loss must be accidental in nature and not done with the intent of creating a situation just to “collect the insurance proceeds”.

3. The loss must be significant when compared to the initial cost of the policy. As an example: Your death benefit is $1,000,000 and the annual premium cost is $1,000. The loss, represented as the death benefit, is significant when compared to the cost ($1,000 a year). This is also known as an aleatory contract. Another way to say this is, the premium is less than the company agrees to pay in the event of a loss.

4. The loss must be measurable and due to chance, outside the control of the insured.

5. The loss must be caused by a non-catastrophic cause, which means the following situations would usually be eliminated from policy coverage; Insured persons in the National Guard while in a “War Zone or in a Foreign Country Police Action”.

Insurable Interest

1. An insurable interest will exist if a loss of property will result in a financial loss to that individual.

2. Examples of someone having an insurable interest is;

   • person owning property
   • person having a lien on the property
   • person living on the property
   • person owed money by the owner
• banker (mortgage holder)
• family

REMEMBER: INSURABLE INTEREST MUST EXIST AT TIME OF LOSS

Indemnity Insurance Contracts

All property and casualty insurance contracts are contracts of indemnity and their purpose is to make the insured “whole again” or pay him/her back. The purpose is to put the insured back in the same financial positions as he/she was prior to the insured loss.

Types of Insurers

Stock Company Insurers: Owned by shareholders just like shareholders of AT & T and General Electric. Shareholders share the profits of the company when and if a dividend is declared. This type of dividend represents profits, not a return of invested capital.

Mutual Company Insurers: The owners of this company are the policy owners, not shareholders. Policy owners may receive dividends, but unlike a stock company dividend, the dividends represent a return of premium, which is based on factors, which will be discussed later.

Non-Profit Service Organizations: Examples include Fraternal Organizations such as the “Royal Elk of Palatine”, HMOs, PPOs and Blue Cross and Blue Shield.

Reinsurers: These companies insure insurers by accepting the transfer of a portion of or all of the risks, which the original company has insured.

Legal Parts of a Contract

1. The Offer: The insurance company, through its agents, will attempt to solicit invitations for offers (THEY DO NOT MAKE THE OFFER) through advertisements, telephone calls and conversations. The prospect makes the offer by filling out the application and submitting it to the insurance company.

2. Acceptance: After the insured submits the application and the initial premium is paid, it is up to the insurance company to accept the offer by issuing the policy.

3. Consideration: All parties in all contracts must provide some form of consideration (something of value) to make the contract valid. The
insured pays the premium while the insurance company makes a promise to pay a covered claim in the future. A contract in which one party, the insured pays something, and the other party, the insurance company, promises to do something in the future, is known as a **Unilateral Contract**.

4. **Contract must be for a legal purpose.** As an example, you can’t buy a policy with the intent to kill the insured to collect the proceeds.

5. **Parties must be competent and understand all the terms:** If your prospect only understands a foreign language, you must provide a means to interpret the terms of the contract or there won’t be a valid contract.

### Parts of The Insurance Contract (D - I - C - E)

**Part I - Declarations**

- Name and address of insured/owner
- Subject of insurance (i.e. Individual life insurance)
- Policy period dates
- Premiums and rates
- List of coverage

**Part II - Insuring Clause**

- Describes the obligations of the insurance company.
- Package policies provide individual insuring agreements for each covered form
- Described are the perils covered and risks assumed

**Part III - Conditions**

- Describes what both the insured and insurer must do in regard to their rights and duties.

**Part IV - Exclusions**

- If the insurance company is going to exclude any type of coverage it must be **specifically** listed in the exclusion part of the insurance policy contract or it cannot be excluded.
More Boring Terms & Definitions

1. **Warranty:** Provision in the insurance policy that pledges that a certain condition does or does not exist. (i.e. “No heart disease problem”)

2. **Concealment:** Failure to disclose a **MATERIAL FACT** that the underwriter, if had known, would not have issued the policy.

3. **Binder:** A temporary contract of insurance, oral or written, offered by an insurer pending issuance of the policy. It is usually written for a period of 30 or 60 days and remains in force for that period unless canceled or a permanent policy is issued or refused by the insurer.

   **Example:** You purchase a new car, call your insurance agent and the agent tells you that your are covered. This is an example of a binder.

4. **Misrepresentation:** A false statement made by the insured such as indicating that he/she doesn’t smoke when in fact the prospect smokes three packs a day. Remember, all answers to all questions asked on the insurance application are considered representations. If an answer is not true it would be a misrepresentation.

5. **Policy Riders:** Riders can only be added to an existing policy and they modify coverage by adding to, or taking away policy coverages.

6. **Aleatory Contract:** A contract in which values are exchanged for unequal values.

7. **Unilateral Contract:** All insurance contracts are unilateral as one party, the insured, pays the premium and the other party, the insurance company, makes a promise to pay in the future if the insured/owner submits a valid claim or wants to surrender the policy. (Act for a promise)

8. **Adhesion Contract:** All insurance contracts are contracts of adhesion because they are written and printed by the insurance company and the courts, if an ambiguity exits, will decide in favor of the insured if any changes to the policy were handwritten or typewritten. These will prevail over the original printed terms. If asked, handwritten changes will prevail over typewritten changes.

9. **Executory.** One of the parties to the contract has duties, which are unfulfilled but still needs to be done.
10. Waiver: Giving up of a known right.

11. Estoppel: The legal term used when an insurance company is denied its right to challenge in court a claim because, by its actions waived a previous rule.

12. Errors & Omission Insurance: Professional liability insurance in which the insurer will defend lawsuits covered by the policy for insurance producers.

13. Certificate of Insurance: This is a document that evidences the existence of insurance coverage.
   - In property insurance a certificate of insurance may be used to demonstrate the existence of a master policy which provides protection for more than one person.
     
     **Example:** A condominium association may have a master property insurance policy insuring the buildings in a condominium complex. Certificates may be issued to each member as proof of their insurable interest.
   - In casualty insurance a certificate of insurance is generally issued to demonstrate proof of liability coverage for a specific location or project.
     
     **Example:** A contractor may be required by the property owner to provide proof of general liability insurance for his/her work.

14. Proximate Cause: An act through an unbroken series of events that can be determined to be the immediate or actual cause of the loss.

   **Example:** Everyone eating catfish in a restaurant gets ill. Even though these patrons did something else after leaving the restaurant, the fact is that they were served food, which was the proximate cause of the injury (sickness).

15. Endorsement: A form added to an insurance contract, which modifies the underlying coverage.

Agency Law

As a licensed insurance producer you will be representing an insurance company with various types of agency authority.
1. **Express Authority**: The agent is told exactly what to do. An example of this is giving the agent specific authority to collect premiums from the insured.

2. **Implied Authority**: While the agent isn’t told specifically what to do it would be okay if the actions of the agent would be acceptable as a reasonable business practice. A good example of this is when the insurance company supplies a receipt book for the agent but doesn’t specifically tell the agent he/she has authority to collect premiums. It would be obvious to a reasonable person that the insurance agent had the authority to collect the premium.

3. **Apparent Authority**: This is the toughest to identify. It may appear that the agent has authority because of certain actions by the agent, and then an innocent third party relies on these actions.

   i.e. After an insurance producer is terminated by an insurance company for lack of production, the agent continues to sell policies. By the way, the insurance company failed to collect any of the forms, business cards and applications, which the agent had. The agent collects a premium and properly follows the conditional receipt rules (to be discussed later) and the proposed insured dies. Will the company have to pay the claim after normal underwriting? Maybe! We’ll leave this up to the courts but this is a good example of the use of Apparent Authority because the proposed insured had no idea that the agent was terminated because the agent had all the “right” materials.

*Insurance Company Functional Departments*

- **Sales**: Markets insurance products
- **Actuarial**: Responsible for keeping the company financially sound by scientifically arriving at death benefit tables, payout options etc.
- **Underwriting**: Responsible for appropriate risk selections, reviewing all applications, sending for needed additional information such as property inspections etc.
- **Claims**: Collects and pays claims
- **Administrative**: Issues policies, billing, policy changes, reinstatement of policies etc.
- **Others**: Legal, advertising, data processing, public relations etc.
Types of Agents

Agents always act in a **Fiduciary Capacity**, which means they must always use utmost care in handling clients and client transactions.

- **Independent Agents**: Contracts with several insurance companies.
- **Captive Agents**: Can only represent one company (i.e. Allstate)
- **General Agent (GA)**: Gets a geographical area and receives overrides for agents writing a particular insurance company policy in that area.
- **Direct Writing Companies**: Insurance company owns the business and have their own employees contact customers directly.

Tort Law - The Law of Legal Wrongs

1. **Intentional Act**: Insurance company will not cover this type of claim. An example may be when a beneficiary intentionally murders the insured.

2. **Negligence**: Failure to do what a reasonable person would do under similar circumstances. Was there a legal duty to act or not to act? Was there a breach of that duty? Was there injury or damage to another person? Was the act the proximate cause of the damages? If all the questions can be answered with a yes then a case for negligence can be made and typically insurance will pay for the covered losses.

- **Strict or Absolute Liability**: It doesn’t matter what or who caused the wrong. The party doing the act is strictly responsible for the results. (i.e. contractors who dynamite buildings - people who have tigers as pets and the tigers attack curious children)

- **No-Fault Insurance**: This is a modification of no-fault insurance as it exists in some states such as New York. It preserves the right to sue another party under certain circumstances unlike true no-fault insurance, which doesn’t allow any lawsuits.

Insured

The insured is defined in every property and casualty policy. A party not specifically named as an insured has no legal right to recover di-
rectly under a policy even if that party has an insurable interest in the insured property at the time of loss. Keep in mind, however, that it is possible for a person not specifically named in the contract to still have recovery rights in the event of loss such as a guest staying at your house. This guest is covered for specific types of loss under dwelling and homeowner’s forms.

**Duties of the insured**

- give notice of claim immediately (written or by telephone)
- prevent further loss as reasonably possible
- separate damaged from undamaged property to determine loss
- inventory the loss
- prepare a proof of loss which is required by the insurer within a reasonable time period, usually 60 days
- make all books and records pertaining to the loss available to the insurer

**Duties of the insurer**

- respond to the insured’s claim in a timely fashion
- evaluate the claim
- treat the insured fairly
- provide repair or replacement cost

**Mortgage Rights**

The mortgagee (bank/lender) has an insurable interest in mortgaged property. The mortgagee must be given an opportunity to file a proof of loss etc. under the policy if the insured fails to do so.

Additionally, the mortgagee is given 10 days written notice of cancellation or nonrenewable if the insurer decides to cancel or not renew the policy.

If the insured fails to provide proof of loss, a mortgagee has 60 days from receiving notice of the failure to file such a proof of loss to file the loss themselves.

**Underwriting**

Underwriting is the process by which prospective insureds are reviewed or examined for their acceptance or rejection. The purpose of underwriting is to pool similar pure risks, not dissimilar ones so that
losses can be predicted with a degree of accuracy. *(Avoid adverse selection)* Premiums can be determined accordingly.

**Loss Ratios**

A loss ratio is the numerical description of the relationship of:

1. *An incurred loss* is a loss which has occurred during a specific period of time such as a calendar year; and

2. *Earned premium* is premium which has been allocated to an insurer’s loss experience, general expense and profit.

**The loss ratio formula can be written as follows:**

\[
\text{Loss Ratio} = \frac{\text{incurred losses}}{\text{earned premiums}}
\]

If an insurer’s incurred losses are greater than the amount of earned premium, the insurer is losing money. In short, loss ratios are numerical indicators of the quality of an insurer’s underwriting.

**Field Underwriting**

Insurance producers have the initial responsibility for evaluating or field underwriting specific business. Insurance producers are the first representatives of an insurer to come in contact with a prospective insured. If a producer feels that a prospect does not fit within an insurance company’s underwriting guidelines he/she must inform the company of same and detail the reasons and possible solutions.

**Corporate Underwriting**

The proposed insured’s application will be reviewed by the insurance company underwriters to determine whether there is an insurable risk, whether there is an insurable interest and whether the property is insurable.

**Factors looked at by underwriters**

- inspection reports
- motor vehicle reports
- credit reports
Fair Credit Reporting Act

This federal act helps insure that applicants for insurance are treated in a fair, accurate and confidential manner. It is the producer’s responsibility to explain the terms of this Act. The signed forms will give the underwriters authority to investigate the proposed insured further if they deem it necessary.

The Act also provides consumers with an opportunity to find out information that an investigative agency has used about them and to whom such reports have been made.

Deposit Premium/Audit

A deposit premium (initial premium) is a tentative charge made at the beginning of certain policies and reinsurance agreements, to be adjusted when the actual earned charge has been later determined. An audit is the verification of books or accounts to determine their accuracy.

A premium computation method of deposit premium and audit is used in a variety of commercial property and liability contracts.

Audit premiums are due and payable on notice. If the sum of the advance and audit premiums paid for the policy term is greater than the earned premium, the insurer will return the excess to the first named insured.

The important concept to remember is that a deposit premium is required for many commercial insureds which is based on an estimate of their risk exposure (payroll or receipts). Thereafter, the insurer will compute the earned or final premium for the audit period in question.

Policy Delivery and Service

Delivering the policy not only means that the policy is physically delivered to policy but that the issued policy is the same as the one that was applied for. It is always best, just like in life and health insurance, to personally deliver the policy. Personal delivery allows you to review the policy terms with the insured to avoid any misunderstandings and confusion. It can also allow you to ask for referrals.

Service of the policy for you client should include the following:

- Maintaining of accurate records
- Advising your clients of anything that should mandate the updating of their policies
- Help clients file claims
- Review existing coverages
2  Property Insurance Definitions & Terms

Introduction To Property Insurance

Property insurance is purchased to cover real property (land) and or personal property (property other than land) against loss or damage from covered perils.

This first section will help introduce you to terms and definitions dealing with property insurance.  Some of these terms were already reviewed in chapter one, but, as they are important we will review them again.

Indemnity

All property and casualty insurance contracts are contracts of indemnity and their purpose is to make the insured “whole again”, not to profit. The purpose is to put the insured back in the same financial positions as he/she was prior to the insured loss.

Replacement and Actual Costs

Replacement Cost (RC)

This is the exact amount of money needed to replace damaged or destroyed property at the point the loss occurred with one of like kind and quality. As depreciation is not a factor, this represents a departure from indemnity rules.

Actual Cost Value (ACV)

Actual cost represents replacement cost less depreciation.

Example: If a chair were destroyed in a covered loss and settlement were to be made on an ACV basis, the cost of the chair in today’s market place would have to be determined first and then a deduction would be made that represents depreciation.

However, if the same chair were destroyed and the policy provided for RC then no deduction would be made for depreciation.

Reality provides us with the fact that buildings insured under property contracts usually are insured on a replacement cost basis as they usually increase in value over time while contents of
the building are usually covered under a ACV basis because of depreciation.

**Limit of Liability**

This is the maximum amount the insurance company is obligated to pay for any loss as specified in the insurance contract. This limit will govern settlement decisions. In most cases, the insurance company will never pay more than the face amount of the contract, which is the coverage as listed in the declarations part of the insurance contract.

**Types of limits**

1. **Split limits:** This provision provides separate payments for losses sustained from limits for bodily injury, property damage and per individual while offering a greater payment for “all individuals’ in an occurrence.

2. **Aggregate limits:** Maximum overall limit for the entire policy period.

3. **Combined single limit:** Offers maximum coverage and is less restrictive to an individual loss then split limits. This will apply on a per occurrence basis.

**Coinsurance**

Coinsurance is found in many property policies in order to require policyholders to carry adequate insurance on their property. A coinsurance clause is an agreement between the insurer and insured in which:

- the insurer agrees to provide a reduced premium rate for coverage;
- the insured agrees to carry a specified percentage of the replacement cost of the building

A typical coinsurance clause of a property policy will state that an insured has to satisfy an 80% level. This means that the insured must carry insurance equal to at least 80% of the value of the insured property.

If the coinsurance clause is satisfied, partial losses will be paid in full. If the coinsurance clause is not satisfied, partial losses will be subject to a penalty payment.
Settlement Formula

Formula:
\[
\frac{\text{Amount of Insurance Carried (} L \text{ )}}{\text{Amount of Insurance Required (} R \text{ )}} \times \text{Loss (} L \text{ )} = \text{Settlement (} S \text{ )}
\]

Example #1:
Market value of an insured building is $200,000
Coinsurance % = 80%
Loss = $40,000
Amount of Insurance = $160,000

Let's work out the numbers!
\[
\frac{$160,000}{160,000} \times \frac{40,000}{40,000} = \text{Settlement ($40,000)}
\]
As the amount of insurance carried is the same as the amount required, the $40,000 loss will be paid in full.

Example #2:
Same facts as in example #1 except the amount of insurance carried is $120,000 instead of $160,000.
\[
\frac{$120,000}{160,000} \times \frac{40,000}{40,000} = \text{Settlement ($30,000)}
\]

Example #3:
Same facts as in example #1 except the building burns down and is totally destroyed. Would the insured receive the full value of the building of $200,000?

Of course not! The insured will never receive more than the applicable limit of liability, in this example $160,000.

Settlement Rules
- The amount paid cannot exceed the limits of the insurance policy
- The amount paid cannot exceed the actual amount of the loss
- The amount paid cannot exceed the dollar amount determined by the coinsurance formula
Extensions of Coverage

If an insured satisfies the coinsurance clause he/she may elect to provide a certain amount of his/her coverage to property not normally covered by the policy as extensions of coverage.

Examples:

- Personal property of others
- Outdoor property
- Newly acquired property
- Constructed property
- Papers and records
- Off premises property

Additional Coverages

Additional coverages provided under a property policy that are in addition to the main coverages. Some examples of additional coverages include the following;

- Reasonable repairs
- Removed property
- Removal of debris
- Loss by forgery
- Trees shrubs and plants

Pair and Set Clause

This clause in a policy will explain how a claim should be handled when one item of a pair or set is damaged. Loss to one item of a pair or set does not constitute loss to the entire pair or set.

The following options may be used;

1. Pay the difference between the actual cash value of the property before and after the loss or;

2. Repair or replace any part to restore the pair or set to its value before the loss

Cancellation

Either the insured or insurer may cancel provided coverage. Each property and casualty policy details the reasons for which the insurer can cancel the policy. Of course these reasons must be in compliance with individual state laws.
While the insurance company must give some specified written notice required by the state, the insured, on the other hand, can request immediate cancellation, without any notice.

If the **insurance company cancels the policy** any unearned premium will be returned on a pro rata basis. There is no allowance for deductions such as service fees. This allows the insured to get back all of the money which has not been used or applied to premium cost.

If the **insured cancels the policy** any unearned premium will be returned on a short rate basis (with deductions made for servicing the policy, etc.) With the short rate basis the insurance company can recoup some of the costs of underwriting and policy processing.

**Appraisal**

When and if both the insured and the insurer cannot agree on a settlement amount each is required to obtain an independent appraisal and share in the cost of an umpire to settle the dispute. The decision of the umpire is final and binding. The issue here is the amount of settlement not whether coverage exists or not.

**Assignment**

This is the transferring of some or all of the rights from one party to another. Assignment of rights and coverages is not permissible under property contracts without the written consent of the insurance company. As an example, owners of a home cannot transfer his/her homeowner’s insurance policy when selling the home.

**Subrogation**

This is the process which allows the insurance company, after paying its insured for a loss, to step into the shoes of the insured as stipulated in the insurance contract in order to recover from third parties any recoverable loss which was reimbursed by the insurance company to the insured.

Subrogation reminds us that the idea of collecting twice for the same loss is not allowed under the doctrine of indemnity.

**Example:** An insured sustained $2,000 property damage to her auto as a result of a rear end hit. The insured could decide to collect for this damage under her collision coverage and collect the amount of the loss less any deductible. Then the insurer assumes the insured’s right of recovery against the responsible third party for the full $2,000.
If the insurance company was not allowed to go against the third party then the insured would collect an additional $2,000 amounting to making a profit on the incident.

**Pro Rata Liability (Other Insurance)**

When more than one insurance company is used to insure a piece of property, pro rata liability rules will apply. This is done in keeping with the doctrine of indemnity. The formula to establish settlement contributions is as follows:

\[
\text{Company Coverage Amount} \times \frac{\text{Loss}}{\text{Total Amount of Insurance}} = \frac{\text{Amount Company Will Pay}}{}
\]

*Example:* Paco, a hard working author, purchases a retreat home in upstate Wisconsin. As a writer, Paco needed plenty of seclusion. Unfortunately, with seclusion comes a number of problems such as a lack of fire hydrants on every corner. Paco attempted to purchase a full coverage insurance policy for his $300,000 home from Lake in the Hills Insurance Company. Unfortunately, the Lake in the Hills insurance company would only provide insurance for $150,000 (Policy A). Paco then went to the Elgin Insurance Company and picked up a policy (Policy B) for the remaining $150,000.

What would happen if there is a $50,000 loss? Will both companies pay the $50,000? Well, we know for sure that both companies won’t pay the $50,000 because of the doctrine of indemnity. Let’s take a look at what the companies will pay under pro rata liability:

- **Policy A = $150,000**
  \[
  \frac{150,000}{300,000} \times 50,000 = \frac{25,000}{50,000}
  \]

- **Policy B = $150,000**
  \[
  \frac{150,000}{300,000} \times 50,000 = \frac{25,000}{50,000}
  \]

**Total Settlement = $50,000**

**Arbitration**

This is a process in which insurance companies usually settle their differences when one company subrogates against another. During this process all parties agree to be bound.
Nonrenewal

This is the act of terminating an insurance policy after the specified policy period. Nonrenewal is a notice given by the insurance company to the insured indicating the intention not to renew the policy upon the normal termination date.

Vacancy/Unoccupancy

Vacancy refers to a building, which is unfurnished, and not being used as a dwelling or for a business.

Unoccupancy refers to a building, which is furnished, but not being used as a dwelling or for business.

Insurance policies treat these differently so make sure you understand the differences and analyze the questions carefully.

Right of Salvage

When an insurance company settles a claim it owns a right of salvage. The insurance company can reduce its losses in the matter by selling the salvage to a salvage dealer. It may determine whether or not property will be repaired, replaced or cash will be provided. In situations where an insured property is not completely destroyed, the insurance company may take possession of it and receive its salvage value when it has replaced or has made a cash settlement to the insured party.

Abandonment

An insured cannot be allowed to abandon the insured property and then demand from the insurance company to be paid in full. The insurance company, by contract, has the right to settle the loss by payment or repair or outright replacement of the property involved.
3 Property Insurance - Dwelling/Homeowners

Dwelling Property Forms

Background

The New York Standard Fire Policy (SFP) has become a standardized model contract. It was designed as a basic policy and not comprehensive. Additional coverage could be added by endorsement.

Dwelling property forms incorporate much of the SFP and Dwelling Buildings and Contents forms, which preceded them. In 1989 a new manual format was established and the program renumbered three policy forms. They are as follows;

- DP-1 (Basic Form)
- DP-2 (Broad Form)
- DP-3 (Special Form)

Dwelling property forms are used to provide coverage for the following types of personal residences;

- one, two, three and four family homes and apartment houses
- dwellings up to five roomers or boarders
- permanently installed mobile homes or trailers

Coverage is Provided as Follows;

DP-1-Direct physical loss caused by;
- fire
- lightening
- internal explosion

DP-2-Direct physical loss caused by;
- fire
- lightning

DP-2 also automatically includes the following extended coverage (EC) perils. These can also be added on to DP-1 by endorsement.

- windstorm (W)
- civil commotion (C)
- smoke (S)
• hail (H)
• aircraft (A)
• vehicles (V)
• volcanic eruption (V)
• explosion (E)
• riot (R)

You can remember them by the acronym **W C SHAVVER**; and

• vandalism and malicious mischief (VMM)

_and the following nine Broad Forms._ Try to remember them by using the acronym **BIG AFFECT**

• burglar damage (B)
• ice and snow weight (I)
• glass breakage (G)
• accidental discharge (A)
• falling objects (F)
• freezing of pipes (F)
• electrical damage (E)
• collapse (C)
• tearing apart (T)

**DP-3**

DP-3 provides coverage for direct physical loss caused by:

• All Risk or Open Perils coverage on the dwelling & other structures
• Broad Form coverage (all 20 perils) - on personal property

**Definitions of Perils**

**Fire**

This has been defined as combustion sufficient enough to produce a spark, flame or glow. Smoke or charring is not enough. Also, it must be a **hostile fire**, not a friendly one. A hostile fire is one that has left it’s intended place such as a log falling out of a fireplace which places the drapes on fire. A friendly fire is one that burns where it was intended to burn such as a fire in a fireplace.
Lightning

A bolt or discharge of atmospheric electricity, which is not man, made. Damage covered by this peril may be the result of lightening itself or the result of a fire caused by the lightening.

Internal Explosion

Covers any explosion occurring inside the described property or other structure containing insured personal property. The following explosions, however, are specifically excluded;

- bursting water pipes
- electrical arcing
- explosions of steam boilers
- rupture or bursting of pressure relief devices

If EC perils are added to the DP-1 endorsement, the explosion peril contained replaces or modifies internal explosion, permitting coverage for explosions originating outside as well as inside the described premises. An additional premium would be required. (See 3.4)

Extended Coverage Perils Definitions

Windstorm

This would include the direct action of wind including objects hurled through the wind that cause damage because of the direct action by the wind. If the insured leaves a window open and something breaks there would be no coverage. The following outside property would be excluded from coverage;

awnings
signs
antennas
rowboats
canoes

Civil Commotion

This can be defined as an uprising or disturbance by a large number of people.

Smoke

Under the DP-1 alone, only smoke from a hostile fire would be cov-
ered. By adding the EC endorsement, the smoke peril is broadened to include any sudden, accidental damage from smoke, with two exceptions:

industrial operations
agricultural smudging (burnoff of growing materials)

**Hail**
Damage caused by the direct action of hail to insured property. If a window is left open and damage occurs, there will be no coverage. Exclusions to hail damage would include;

frost
cold weather
snow
sleet
ice
rain

**Aircraft**
Coverage provided for damage caused by aircraft, including self-propelled missiles, spacecraft, airplane, dirigible, balloon, helicopter etc. I’m sure you remember reading about “blue stuff” falling from the air. Keep in mind that this peril would also apply to damage caused by the falling of an aircraft or the falling of a part or object from an aircraft.

**Vehicles**
This peril provides protection for any damage caused by a vehicle to the covered property. Exclusions include damages caused by vehicles owned or operated by the insured, damage to fences, driveways and wooden walks.

**Explosion**
Under EC, explosions are covered whether they originate inside or outside the building. Exclusions include bursting from water pipes, electrical arching, rupture or bursting or pressure reduction devices, explosions of steam boilers or steam pipes.

**Riot**
Under legal definitions riot is defined as the assemblage of three or more people, which results in the use of force or violence against indi-
individuals or property. Coverage includes direct loss caused by striking employees. Riot and civil commotion can be probably be defined as being the same or nearly the same.

**Volcanic Eruption**

This includes losses caused other than by earthquake, land shock waves or tremors. This peril will cover damage caused by the eruption of a volcano including the ensuing lava flow and airborne particles.

**Vandalism and Malicious Mischief (VMM)**

This includes any willful and malicious damage or destruction except theft and glass breakage. To get coverage these acts must be intentional. With DP-1, if the EC perils are purchased VMM coverage can be purchased. Under DP-2, EC perils and VMM are provide automatically.

**Broad Form Perils (B-I-G-A-F-F-E-C-T)**

**Burglar Damage**

This covers damage done to the property but not to any property taken.

**Ice**

Protection is provided from falling objects such as ice, snow and sleet. Damage to the insured building and/or contents due to their weight is covered. Coverage does not extend to the following;

- awnings
- fences
- patios
- pavements
- swimming pools
- foundations
- retaining walls
- bulkheads
- wharves
- docks
- piers
Glass Breakage

All building glass as long as the insured premises has not been vacant for 30 consecutive days or more immediately before the loss.

Accidental Discharge

Accidental discharge of water and steam from plumbing, heating, air-conditioning or fire protective sprinkler systems, or of a household appliance. This does not include losses due to continuous leakage or seepage. No coverage for a building unoccupied for more than 30 consecutive days immediately before the loss or to the system or appliance causing the water or steam escaping.

Falling Objects

Covers damages to the exterior of the insured premises and its contents if the falling object first damages the roof or exterior wall. Damage to the falling object itself is not covered. Outdoor antennas, wiring, equipment, awnings and fences are not covered.

Freezing of Pipes

Losses not covered if the dwelling is vacant, unoccupied or being constructed unless the insured has taken reasonable care to;

- maintain heat in the building; or
- shut off the water supply and drain the system

Electrical Damage

Coverage from sudden and accidental electrical current.

Collapse

The collapse peril covers risk of direct physical loss to covered property involving collapse of a building or any part of it caused by;

- perils insured against in the policy
- hidden decay
- insect damage
- weight of contents
- weight of rain collected on the roof
- use of defective materials
The collapse does not include:

- settling
- cracking
- shrinking
- bulging
- expansion

The following are exclusions:

- awnings
- fences
- patios
- swimming pools
- underground pipes, drains and septic tanks
- foundations

**Tearing Apart**

Sudden and accidental tearing apart, cracking, burning or bulging of steam or hot water heating systems, air-conditioning, or automatic fire protective sprinkler systems or hot water heaters. This peril does not include loss caused by freezing except as provided in the peril of freezing.

**Dwelling Property Special Form (DP-3)**

This is an all risk or open perils policy unlike DP-1 and DP-2 which are written on specific perils. DP-3 is defined by its exclusions. If a peril is not specifically excluded then it is included. If contents are covered under DP-3, they are insured against the same perils as provided under the DP-2. So, DP-3 provides All Risk or Open Perils coverage on the dwelling and other structures and Broad Form coverage on personal property.

**Dwelling Property Coverages**

The dwelling property forms can provide coverage for the following property:

- Coverage A - Dwelling
- Coverage B - Other structures
- Coverage C - Personal property
- Coverage D - Fair rental value
- Coverage E - Additional living expenses
Coverage A - Dwelling

This includes materials and supplies used in construction repair or alteration of a dwelling and other structures. Building equipment and outdoor equipment which is not covered as personal property, but is located on the premises, is included.

Land is not included in this coverage. The insured can purchase coverage on the dwelling only, or contents only or both dwelling and contents.

Coverage B - Other structures

This provides coverage for structures which are not attached to the dwelling, such as a tool shed, detached garage or any other out-building on the premises whose use is incidental to the maintenance of the main dwelling. Under all property forms, DP-1, DP-2 and DP-3, 10% of the dwelling amount is the maximum coverage for loss to other structures listed in the policy.

Under DP-1 the 10% is not an additional amount of insurance but is included in the total coverage under Coverage A. In DP-2 and DP-3 forms, coverage is increased by 10% over the policy limits.

Example: If an insured has $100,000 in coverage, 10% of the $100,000, or $10,000 can be applied under DP-1 unless the full $100,000 is used to pay off the claim. In which case there would be nothing left because of Coverage A. On the other hand, under DP-2 and DP-3, $10,000 would be available over and above the $100,000 policy as additional insurance.

Coverage C - Personal Property

Personal property which is normally in the dwelling is covered up to 10% of the policy limit under Coverage A. A basic form reduces the coverage A limit for any Coverage C claims, but is paid in addition to Coverage A amounts in both broad and special form coverages. The following are specifically excluded from coverage:

- accounts
- bills
- currency etc.
- manuscripts
- birds and fish
- money and securities
- deeds
• aircraft and parts
• boats other than row boats and canoes
• motor vehicles unless used to service the premises

If personal property is moved to a new residence, coverage applies automatically at the new location for 30 days. Coverage extends to the personal property of a named insured and personal property belonging to any member of the family living at the named premises.

**Coverage D - Fair Rental Value**

This insures against the loss of the fair rental value of any part of the insured premises rented to others or held for rental. Payment will be for the shortest time required to repair or replace that part of the described location rented or held for rental. Under DP-1, the insured may apply 10% of the dwelling amount to cover Fair Rental Value with an internal monthly maximum of $1/12$. A total loss would preclude coverage. Under DP-2 and DP-3, there is no $1/12$ limitation.

**Coverage E - Additional Living Expense**

Coverage is provided to the insured and family while the insured property is unfit for use. Coverage is the same as indicated in D above regarding DP-1, DP-2 and DP-3.

*Note:* Property which is removed in order to protect it is insured against direct loss from any cause for **5 days** under the basic form (DP-1) and up to **30 days** for the broad and special form.

**Dwelling Property Exclusions**

• war
• nuclear hazard
• water damage
• earth movement
• power failure
• ordinance or law
• neglect
• intentional loss

*War:* excludes all items of damage relating to war or warlike actions.

*Nuclear Hazard:* Losses due to radiation or radioactive contamination.
**Water Damage:** Includes floods, surface water, tidal waves, overflow from streams, water below the surface of the ground including seepage or leaks through sidewalks, walls, basements, floors or windows.

**Earth Movement:** This means earthquakes, tremors, shocks or movement of the earth unless direct loss occurs by fire or explosion.

**Power Failure:** Power interruption can cause losses in many ways. But, these types of losses are excluded unless the interruption is caused by a covered peril or covered item. The equipment must be located on the insured's premises and damage to that equipment must be caused by an insured peril.

**Ordinance or Law**

Ordinance or law requiring the construction repair or demolition of property is excluded.

**Neglect:** This means the insured’s unwillingness to use all means available to save and preserve his/her damaged property from further loss.

**Intentional Loss:** It applies to losses caused and intended by the insured.

**DP-3 Special Exclusions**

In addition to the exclusions listed above, the following are DP-3 specific exclusions caused by the following perils;

- wear, tear, deterioration, rust, mold and rot
- smoke from agricultural smudging or industrial operations
- latent defects
- smog
- mechanical breakdown
- birds, rodents, insects or domestic animals
- settling, cracking, shrinking, bulging, expansion
- wind, hail, ice, snow or sleet damage to antennas, lawns, plants, shrubs and trees
- freezing, thawing or damage caused by the weight of ice, snow or sleet to awnings, fences, pavements, patios, swimming pools, foundations, retaining walls
- theft of property not actually part of the insured building
- vandalism and malicious mischief, burglary and glass breakage if the dwelling has been vacant for more than 30 consecutive days
Dwelling Property Conditions/Coverages

**Mortgage Clause:** The mortgage clause acknowledges the insurable interest of the mortgagee (holding the mortgage). The mortgagee’s insurable interest in a dwelling is the amount of money owed by the insured on the dwelling.

**Liberalization Clause:** Agrees to provide existing policies with any liberalization that revised editions of the same policies might offer.

**Reasonable Repairs:** In the event that covered property is damaged by an insured peril, the insurer will pay the reasonable cost incurred by the insured for necessary measures taken solely to protect against further damages.

**Debris Removal:** Insurer will pay to remove debris if a peril insured against causes a loss.

**Trees, Shrubs and Other Plants:** Provides coverage for losses caused by fire, lightening, explosion, riot, aircraft, vehicles not owned by the insured, vandalism, malicious mischief, etc. Limit of not more than 5% of Coverage A and is considered additional insurance. Any one tree or shrub - maximum of $500

**Fire Department Service Charge:** Policy will pay up to $500 if fire department called to protect property.

**Concealment or Fraud:** Policy is void if insured intentionally conceals or misrepresents a material fact, engaged in fraudulent conduct or made false statements.

**Recovered Property:** Loss payment will be adjusted based on the amount the insured received for the recovered property.

**Settlement Considerations:** All DP-1 losses, whether for the dwelling or personal property, are settled on a Actual Cost Value basis, while DP-2 and DP-3 are settled on a Replacement Cost basis. If the insured does not carry at least 80% of the full replacement cost of the building the following formula must be used:

\[
\text{Insurance Carried} \times \frac{\text{Loss}}{\text{Insurance Required}} = \text{Settlement}
\]

**Example:** Dwelling would cost $200,000 to replace. It’s insured under a DP-3 for $120,000. Under contract terms the insured should carry 80% of
$200,000 or $160,000. In the event of a $20,000 loss the insured will receive $15,000.

\[
\frac{120,000}{160,000} \times 20,000 = 15,000
\]

**Review Chart On Comparison of the Dwelling Forms**

<table>
<thead>
<tr>
<th>Coverage Form</th>
<th>Basic (DP-1)</th>
<th>Broad (DP-2)</th>
<th>Special (DP-3)</th>
</tr>
</thead>
<tbody>
<tr>
<td>A Dwelling</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>B Other structures</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>C Personal Property</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>D Rental Value</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>E Living Expenses</td>
<td>Yes</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Extended Coverage</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td># of Extensions</td>
<td>7</td>
<td>9</td>
<td>9</td>
</tr>
<tr>
<td># of Days for removal</td>
<td>5</td>
<td>30</td>
<td>30</td>
</tr>
<tr>
<td>Perils Covered</td>
<td>Fire</td>
<td>Fire</td>
<td>All risk for Coverage A &amp; B and Broad Form Perils for personal property (Coverage C)</td>
</tr>
<tr>
<td></td>
<td>Lightning</td>
<td>Lightning</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Internal</td>
<td>EC &amp; V &amp; MM</td>
<td></td>
</tr>
<tr>
<td></td>
<td>Explosion</td>
<td>8 more (4 for outside and 4 for inside)</td>
<td></td>
</tr>
<tr>
<td>Basis Of Recovery</td>
<td>Actual Cash Value</td>
<td>For Buildings Replacement Cost if 80% Insured to value All other - ACV</td>
<td>For Buildings Replacement Cost if 80% Insured to value All other - ACV</td>
</tr>
</tbody>
</table>

**Note:** EC and V&MM Perils are optional for the Basic Form and will only be applied if premium for them is shown on the policy.

**Homeowners HO Forms**

Homeowners coverage is identified as HO Forms. The HO stands for Homeowners. The homeowners policy is a multi-line policy. It combines property (fire) coverage with casualty (personal liability and theft) into a single contract.
Homeowners policies are divided into two areas that define coverage. **Section I** applies to coverage of property and **Section II** which provides coverage for legal liability. Section I will vary according to the HO form below while section II will be identical in all forms. These will be discussed in detail following the HO forms.

The six Homeowners forms are:

- HO-1  Basic
- HO-2  Broad
- HO-3  Special
- HO-4  Tenant Broad
- HO-6  Condominium or unit owner
- HO-8  Modified Coverage
- HO-15 Special personal property endorsement (Must attach to a HO-3 only)

Note: The HO-1 form has been discontinued in many states and replaced with an HO-8.

The greater the HO number the greater the coverage other than HO-6 and HO-8 which does not provide coverage for private residences. **The HO contract** is available to premises which are used for **private residences**, containing no more than two families and no more than two boarders or roomers per family. A **Mobile Home Endorsement (MH-200)** may be added to an **HO-2 or HO-3 policy** if the mobile home is designed for year round living.

**HO-1** provides coverage for direct physical loss caused by:

- fire
- lightning
- EC Perils
  - windstorm  (W)
  - civil commotion  (C)
  - smoke  (S)
  - hail  (H)
  - aircraft  (A)
  - vehicles  (V)
  - volcanic eruption  (V)
  - explosion  (E)
  - riot  (R)
- vandalism and malicious mischief (VMM)
- theft (not by the insured)
HO-2 provides coverage for direct physical loss caused by:

- the Basic HO-1 perils; plus
- the Broad Form perils
  - burglar damage (B)
  - ice and snow (I)
  - glass breakage (G)
  - accidental discharge (A)
  - falling objects (F)
  - freezing of pipes (F)
  - electrical damage (E)
  - collapse (C)
  - tearing apart (T)

HO-3 provides coverages for direct physical loss caused by:

- all risk or open perils - on the dwelling
- HO-2 perils - on the contents

HO-4, HO-6 and HO-8 provide the same perils as the HO-2 coverage with few exceptions. HO-4 is designed for tenants of apartments and provides extensive coverage on the insured’s contents. HO-6 is for condominium dwellers. **HO-8 is a modification of the HO-1 designed for dwelling owners living in areas where home market values are far below the replacement cost of the dwelling.** The most significant difference between the HO-1 and the HO-8 is that the HO-1 is written on a replacement cost basis while the HO-8 is actual cash value. H20 adds on losses and falling objects to the HO-2 policy.

Homeowners Coverages

**Section I - Property**

**Coverage A - Dwelling**

- Dwelling, structures attached, materials and supplies located on the dwelling used for construction, alteration or repair are covered.
- Coverage does not include any land
- Does not apply to HO-4 apartment dwellers
- HO-6 covers alterations, appliances, fixtures within the premises and property which is the insured’s insurance responsibility under a property owners agreement and structures owned solely by the insured other than the principal residence at the residence premises.
Coverage B - Other Structures

- Provides protection for structures on the premises which are detached from the dwelling. (tool shed and a garage)
- HO-6-owned garages or storage buildings are covered for a stated amount
- Coverage does not apply to land or structure used for business or rented to anyone other than a tenant of the dwelling.
- 10% of the amount of insurance written under Coverage A is provided as an additional amount of insurance.

Coverage C - Personal Property

- Provides protection for personal property which is owned or used by the insured anywhere in the world
- 50% of Coverage A is the limit amount for all HO forms except HO-4 and HO-6
- Under HO-4 amount of coverage is based on actual cash value of the contents of his/her apartment
- HO-6 also based on a flat dollar amount
- Exclusions
  ◊ animals, birds and fish
  ◊ aircraft and parts
  ◊ autos or motorized vehicles unless used to service the premises
  ◊ property of boarders not related to the insured
  ◊ property in an apartment which is regularly rented if it is away from the insured premises
  ◊ business property of a business which is conducted on the premises such as business data but blank recording tapes covered
  ◊ music reproduction devices used in vehicles

- Special Coverage C Limits - specific dollar amounts apply to each of the below named categories of personal property and these limits can be raised by endorsement if needed;
  ◊ money (coins and precious metals)
  ◊ securities, accounts, deeds and other valuable papers
  ◊ watercraft
  ◊ stolen firearms
  ◊ stolen jewelry, furs and precious stones
  ◊ business property used away from the premises
  ◊ loss of portable electronic apparatus in autos
Coverage D - Loss of Use

This coverage reimburses for additional living expense and fair rental value when the insured premises is unfit to live in. The coverage pays the additional costs related to living elsewhere and the fair rental value of the insured premises minus noncontinuing expenses.

Coverage D limits are written as a percentage of Coverage A under the HO-1, HO-2, HO-3 and HO-8 and a percentage of Coverage C under the HO-4 and HO-6.

Note: Other additional coverages available include Inflation Guard Endorsement which automatically increases the coverages under A, B, C and D on a regular periodic basis and Replacement Cost for Personal Property as a rider to all HO policies.

Section II - Comprehensive Personal Liability

The insured is covered for his/her responsibility as a homeowner to the general public through Coverage E - Personal Liability and Coverage F - Medical Payments to Others. Coverage is for non-business activities. Conditions include the insured’s location, personal activities of the insured on or off the insured premises and actions of an employee who lives at the insured location in the course of employment. The insured includes the name insured and all related residents of the same household and residence under 21 in the care of any member of the named insured’s family.

Coverage E provides two separate coverages;

- Bodily injury (BI) liability
- Property Damage (PD) liability

Bodily injury includes bodily harm, disease or sickness even if it results in death.

Property damage applies to the physical injury or destruction to tangible property, even including the loss of such property.

Coverage E will also provide a legal defense at the insurer’s choice, even if the suit is groundless, false or fraudulent.

Coverage E - Exclusions
• contractual liability other than relating to ownership or use of the insured location
• BI or PD of an insured
• PD to property rented, occupied or used by insured
• BI to individuals covered by workers compensation or disability insurance

Coverage F - Medical Payments to Others

This coverage pays for the necessary medical expenses accrued within a **three year time frame** from the date of the accident by a guest or others who may be injured on the insured’s premises or as a direct result of an insured’s personal activities.

Coverage F is not limitless. It will pay for;

• medical expenses only including medical and surgical care, x-rays, dental, ambulance, hospital and professional services, prosthetic devices and even funeral services.
• guests and other individuals, but **not the insured** and regular residents of the insured household other than residence employees.
• Coverage F applies to others when they are on the premises with the permission of the insured or off the insured premises if the bodily injury was caused by;
  ◊ a condition on the insured premises
  ◊ an activity of the insured
  ◊ a residence employee (i.e. live in maid)
  ◊ an animal owned by the insured

Coverage F - Exclusions

• to a residence employee not sustained in the course of employment
• to any person eligible to receive workers compensation
• from any nuclear reaction
• to any person regularly residing on the insured premises

Note: In the newer Homeowners forms, Coverage E is written for a minimum of $100,000 and Coverage F is $1,000.

Note 2: Liability and medical payments coverages will be discussed in detail in the Casualty section of this text.
Section I - Additional Coverages

All Homeowners forms provide additional coverages provided in addition to the major Section I - Coverages A through D, but costing no additional premium.

1. Debris removal if a covered peril causes a loss
2. Cost of reasonable repairs to protect the property from further damage
3. Trees, shrubs and plants on the residence premises for losses caused by covered perils - up to 5% but no more than $500 per tree, shrub or plant
4. Fire department service charges up to $500 when the fire department is called to fight a covered peril
5. Property removed from the insured premises endangered by insured peril and covered up to 30 days at a new location
6. Credit card forgery and counterfeit money-pays up to $500 due to the theft or unauthorized use of an insured check or negotiable instrument
7. Loss assessment - up to $1,000 charged by a corporation or association for a direct insured loss to property owned collectively
8. Landlord’s furnishings up to $2,500 for the insured’s (as landlord) appliances, carpeting and other household furnishings in an apartment on the residence premises

Section I - Additional Coverages Exclusions

- ordinance or law
- earth movement
- water damage
- power failure
- neglect
- war
- nuclear hazard
- intentional loss by or directed by an insured with the intent to cause loss

Section I - Additional Coverages Conditions

- **limit of liability** in any one loss for more than the amount of the insured’s interest at the time of loss and the applicable limit of liability
- **After a loss** the insured must notify the company or agent promptly, notify the police in the event of a theft, notify the
credit card company, take reasonable steps to protect the insured property from further damage, make reasonable and necessary repairs to protect the property, keep records of repairs, prepare an inventory of damaged personal property, cooperate with the company by showing damaged property and records and submit a proof of loss within 60 days of the insurer’s request.

- **Loss settlement rules** in which personal property losses are settled on an actual cash value (ACV) basis while buildings insured under Coverages A and B are settled on a replacement cost basis subject to an 80% coinsurance requirement.
- **Loss to a pair or set**
- **Glass Replacement** with safety glazing materials
- **Appraisal**
- **Pro Rata Liability for other insurance**
- **Suit against insurer** requires that all policy provisions have been complied with and the suit is stated within one year of the date of loss
- **Abandonment of Property** not allowed by the insured
- **Mortgage clause** rules same as in the Dwelling Program
- **No Benefit to Bailee** (holder of goods)
- **Nuclear Hazards** excluded
- **Recovered Property** can be kept or turned over to the insurance company

**Section II - Comprehensive Personal Liability Additional Coverage**

- **Claims expenses** for the cost of investigating a claim, premiums for bonds required in a suit the company decides to defend, reasonable expenses incurred by the insured, interest on judgment which accrues after the entry of the judgment.
- **First Aid Expenses** incurred by an insured to others but will not pay first aid expenses for first aid to the insured.
- **Damage to Property of Others** - company will pay the replacement cost of property of others damaged by an insured up to $500 per occurrence.
- **Loan Assessment** - $1,000 per occurrence for the insured’s share or assessment as a member of a group of property owners including liability for an act of a director, officer or trustee

**Section II - CPL Additional Coverage Common Exclusions**

- Coverages E - Personal Liability and F - Medical Payments to others do not apply to bodily injury or property damage arising out of;
◊ BI or PD expected or intended by the insured
◊ business pursuits of an insured
◊ insured’s failure to render professional services
◊ premises which are not an insured location
◊ motor vehicles and watercraft
◊ aircraft
◊ nuclear weapons
◊ transmission of a communicable disease by an insured
◊ sexual molestation

Section II Additional Coverage General Conditions

These will apply to both Sections I and II;

- coverage only during the policy period
- no coverage for insureds who intentionally conceal or misrepresent any material fact relating to insurance coverage
- waivers must be in writing to be effective
- insured may cancel at any time while the insurance company can cancel only for nonpayment of premium and for the first 60 days of coverage or less for any reason and can cancel if the policy has been in effect for 60 days for material misrepresentation or change in risk
- after one year, the company may cancel for any reason on the anniversary date with a 30 days notice
- Coverage will continue after the insureds death

Mobile Homes Coverage

Due to their high exposure to risk and loss, mobile homes are excluded from homeowner policies, with the exception of the availability of the MH-200 endorsement which can be added to an HO-2 or HO-3 policy. If the mobile home is permanently fixed on a foundation then a dwelling policy can be used. Because of depreciation, losses are always based on actual cash value and not replacement value. The mobile home package policy offers broad form of All Risk coverage for the following;

- mobile home, all equipment
- built in accessories
- additional structures such as awnings, carports and shelters
- Collision (optionally available)
- Additional living expenses
Note: Mobile home coverage is available under Homeowners policies if the home is at least 10 x 40 feet and designed for year round living.
4 Property Insurance - Commercial Lines

Overview

Commercial lines property forms are designed to address the various property related insurance needs of businesses. In this chapter we will review commercial property coverages with the Commercial Building and Personal form, insurance for businesses through the use of the Causes of Loss forms, Business Income and Extra Expense forms to provide coverage against indirect or consequential business losses, Commercial Package Policy (CPP) permitting commercial insureds to package their own coverages and finally a commercial package designed for small businesses, the Business owners Policy, policy for manufacturing and other commercial risks, the Boiler and Machinery Policy.

Introduction

Protection extends to businesses that own and occupy their own premises or to businesses that rent or lease space. Businesses who lease tend to make expensive alterations or improvements in order to occupy a premises for a particular purpose. This investment needs to be protected through insurance.

Businesses have an insurable interest in buildings and equipment including fixtures, machinery, furniture and inventory. Important considerations also include consequential or indirect losses due to interrupting a business’s ability to earn money because of a direct loss.

Commercial Property Covered

Building: All buildings, additions and extensions to the buildings as well as permanent fixtures

Business Personal Property: Personal property of the insured used in business to include the following; (other than real property)

- furniture
- fixtures
- machinery
- equipment
- inventory
- all other property used in the business
- labor, materials or services on personal property of others including property in the insured’s care and custody and prop-
Property Not Covered

As the Commercial Building and Personal Property coverage form contains relatively broad definitions of the types of property covered, it is necessary to review what it will not cover:

- valuables
- animals
- automobiles held for sale
- bridges and roadways
- contraband
- cost of excavations and grading
- foundations of buildings
- land
- pilings and docks
- property covered under other coverage
- growing crops
- personal property while airborne or waterborne

Additional Coverage Form

- debris removal
- expenses as a result of preservation of the property
- fire department service charge ($1,000 maximum)
- pollutant clean up and removal ($10,000 per policy period)

Coverage Extensions

80% coinsurance would apply under which the insured may have the following extensions of coverage:

- **newly acquired or constructed property**

  This property is covered up to **25% or a maximum of $250,000** per building. This applies to new buildings being constructed on the insured premises and buildings acquired at a location other than the insured’s premises to be used for the same purpose as the insured’s building or warehouse.

  There is a **10% or $100,000** maximum of personal property applied up to 30 days to cover business personal property at a newly acquired location.
• **Personal Effects**

A maximum of $2,500 will be paid for loss of personal effects of the insured’s officers, partners and employees. This coverage applies to all personal property which could include a calculator, coat, briefcase etc.

• **Valuable Papers**

Up to $1,000 at each described premises can be applied to the cost of researching, replacing or restoring lost information. This can include the existence of magnetic media.

• **Property Off-Premises**

Insured property other than stock damaged or destroyed by a covered peril but will not apply to property in a vehicle, in the care or control of the insured’s salesperson or at any fair or exhibition. Maximum coverage is $5,000.

• **Outdoor Property**

A $1,000 maximum can be applied for outdoor property extensions such as outdoor fences, antennas, signs, trees, shrubs and plants destroyed by fire, lightning, explosion, riot or aircraft. There is maximum of $250 per plant or shrub.

**Causes of Loss Forms**

*Basic Form* provides coverage against the following perils;

- fire
- lightning
- extended coverage (EC)
- vandalism and malicious mischief (VMM)
- sprinkler leakage (automatic sprinkler system)
- sinkhole collapse (collapse into underground empty spaces)

*Broad Form perils*

- the Basic perils above
- breakage of glass
- falling objects
- weight of snow, ice or sleet
- water damage (accidental discharge or leakage from a system or appliance)
- building collapse
**Special Form perils**

- all risk or open perils except as excluded

**Common Exclusions**

- ordinance or law
- earth movement
- governmental action
- nuclear hazard
- off-premises services (power failure)
- war
- water (including flood)

**Special Form Exclusions**

Do not try to memorize the following exclusions. Just try and understand why they are exclusions. Remember, all property will have some wear and tear and as it is foreseeable, it is not insurable.

- artificially generated electric current
- delay or loss of use of market
- smoke or gas from industrial or agricultural smudging
- such cause of loss from;
  - ◊ wear and tear
  - ◊ rust and corrosion
  - ◊ smog
  - ◊ settling, cracking etc.
  - ◊ insects, birds and rodents
  - ◊ mechanical breakdown
- explosion of steam boilers
- continuous leakage of water over 14 days or more
- water leaks from plumbing, heating, air conditioning caused by freezing unless the insured attempted to maintain heat in the building or the insured drains the equipment and shuts off the water supply if the heat is not maintained.
- dishonest or criminal act by the insured, any partners, employees etc.

**Earthquake Form**

**Coverage**

Coverage is provided against earthquake, volcanic eruption and explosion. This coverage includes damage caused by shocks within 168
hours after policy expiration if shocks began during the policy term. Volcanic activity is also covered and will include lava flow, ash and airborne shock waves. Earthquake only coverage is not available.

**Builders Risk**

This policy is written for a period of one year usually on a completed value basis. A condition called “Need for Adequate Insurance” underscores the importance of accurately estimating the final value of the building by placing a virtual 100% co-insurance requirement on the contract. If the actual completion value is higher than the insurance completion amount, then any paid losses are lowered by the resultant difference in value versus actual coverage amount (i.e. the building ends up with a value of $200,000 but was only insured for $100,000. Any loss which is less than total is paid at only a 50% rate by the insurance company).

Coverage begins when construction starts and it stops;

- when the purchaser accepts the property
- 90 days after construction completion
- upon occupancy or intended use of the building
- when the interest of the insured in the property stops
- if the builder abandons construction with no intention of completion

Coverages include the building being constructed, foundation, fixtures, equipment used to service the building, materials and supplies intended to be placed into the building which are within 100 feet of the premises.

**Indirect Loss Coverages**

Because the loss caused by the interruption of business may far surpass the actual physical loss to property, this exposure has been addressed through the development of several consequential or indirect loss coverages.

**Business Income Coverage**

This is also known as time element coverage which pays for the loss of income over a period of time which results from a direct physical loss. The Business Income Coverage Form covers this loss of income due to the interruption of business by an insured peril during the period of restoration.
The loss of income refers to the net income or pretax profit (before income taxes) that a business would have earned plus normal continuing operating expenses, including payroll.

In order for Business Income Coverage to apply, the interruption of business must be caused by direct physical damage to property at the described premises.

The period of restoration begins on the date of the actual physical damage to the insured property and ends on the date when the property should be repaired with reasonable speed and similar quality.

**Additional Coverages**

**Extra Expenses**

These expenses are necessary to continue a business in operation. An example can include renting temporary offices to continue the business so as to reduce further losses.

**Civil Authority**

Under this coverage the policy is extended to cover loss of business income and extra expense for a period up to two weeks caused by a action of civil authority.

**Alterations and New Buildings**

This coverage provides for the actual loss of business income due to direct physical loss by a covered peril to new buildings, alterations, machinery, equipment, supplies used in construction, alterations or incidental to the occupancy of new buildings.

**Extended Business Income**

This automatically extends the period of restoration up to another 30 consecutive days to cover additional loss of earnings as long as the insurance policy limits have not been exhausted.

**Commercial Package Policy (CPP)**

Policies containing a single coverage part is a monoline policy while a policy containing two or more coverage parts qualifies as a package. The new package approach is intended to simplify and standardize the process of assembling policies.
To qualify as a Commercial Package Policy, a policy must contain the Common Policy Declarations Form, the Common Policy Conditions Form and **two more of the following coverage parts:**

- Boiler and machinery
- Commercial auto
- Commercial property
- Crime
- Farm
- Inland Marine
- Commercial general liability
- Pollutant liability
- Products Liability

**Businessowners Policy (BOP)**

This is a policy designed for small and medium sized apartment, office and mercantile risks as an alternative to the Commercial Building and Personal Property Coverage Form. Tenants of offices and stores can insure business personal property. As BOP is a complete package policy by itself, it is not attached to some other coverage or package.

The following processing and service type businesses are also eligible for coverage;

- appliance dealers
- bakeries
- barber shops
- funeral homes
- printers
- photographers

On the other hand the following businesses would **not** be eligible;

- service stations
- auto repair centers
- contractors
- bars
- household personal property
- places of amusement
- wholesalers
- banks and other financial institutions
The BOP is a *multi-peril policy* including basic property and liability coverages. If needed, there are optional coverages that can be used to custom design a policy for the small business.

Property coverage can be written on either a standard or special form. Most coverages of the two forms are identical except for “covered causes of loss”. The standard form is like the basic coverages found in other commercial forms while the special form is all risk coverage. Optional coverage is available to include burglary, robbery, money, securities, outdoor signs, exterior grade floor glass, mechanical breakdown and employee dishonesty.

*Eligibility is available for the following risks:*

1. **Apartment buildings** to include mercantile, service or processing occupancies not in excess of 15,000 square feet and incidental offices. Residential condominium associations are eligible.

2. **Office Buildings** not higher than 6 stories and limited to 15,000 square feet. Office condominium associations are eligible.

3. **Mercantile Risks** with gross sales not exceeding $1 million and having no more than 15,000 square feet of space. Incidental storage buildings or occupancies in connection with an eligible risk and not exceeding 15,000 square feet are eligible.

4. **Service and Processing businesses** with gross sales not exceeding $1 million and having no more than 15,000 square feet in total floor area and incidental storage facilities not exceeding 15,000 square feet.

Businessowner liability coverage form protects against loss from bodily injury, property damage and for personal and advertising injury.

**Boiler and Machinery Insurance**

The Boiler and Machinery policy can be written by itself or in conjunction with a broader commercial lines property coverage. If written on a specific basis, each boiler or machine to be insured is listed and described in a schedule which is then attached to a policy. If written on a blanket basis, all boilers and machines of a certain class are insured. Emphasis of this type of policy is prevention. Prevention of losses are a result of frequent boiler inspections which are carried out by trained engineers.
**Coverage**

Covered property means any property that the insured owns, is in the care, custody or control of the insured and for which the insured is legally liable. The policy promises to pay for direct damage to covered property by a covered loss. Covered causes of loss are accidents to machines shown in the Declarations. An accident is defined as a sudden and accidental breakdown of the insured boiler or machine necessitating repair or replacement of the boiler or machine. An accident does not include any of the following:

- wear and tear
- depletion
- deterioration
- depletion
- corrosion
- erosion
- leakage of a valve
- breakdown of tubes
- breakdown of electronic computers
- breakdown of structures or foundations supporting the boiler or machine
- the functioning of any safety device
- explosion of gas or unconsumed fuel within the furnace or any of its passageways

**Expediting Expenses**

This coverage reimburses the insured for any reasonable extra expenses involved in making temporary repairs and of expediting the repair of the damaged property. Examples can include employee overtime and the extra cost of express shipments. Policy limit is $5,000.

**Defense, Settlement and Supplementary Payments**

This policy will pay all cost of legal fees, interest on judgments and premiums for appeal bonds as is customary for liability insurance coverages. The amount paid by the company under this coverage is in addition to the face amount of the policy.

**Inspection Service**

The company provides periodic inspections of the insured boilers and machines as a free service. These inspections often detect dangerous conditions that can prevent accidents from happening. If an inspection detects an unsafe condition the unit can be shut down.
Small Business Boiler and Machinery Policies

The Basic Form may be written for the following small businesses having insurable boilers and/or machines valued at no more than $5 million.

- apartment buildings
- churches
- motels
- hotels
- office buildings
- garages
- retail stores
- schools
- banks
- restaurants
- nursing homes
- theaters
- funeral homes

Expanded Benefits

The Broad Form expands the eligibility requirements for insurable risks to include much smaller boilers, refrigerator units, air conditioning systems and other mechanical or electrical equipment used for the maintenance or service of the premises.

Marine Insurance

Ocean Marine Insurance

Oldest form of property insurance which provides property coverage in the event of a marine loss to the hull (ship itself), cargo (freight), loss of income and protection and indemnity (liability insurance).

Inland Marine Insurance

This is an outgrowth of Ocean Marine Insurance where coverage was extended to loss from movable property that is transported on land. Some of the risks that may be covered are;

- imports
- exports
- domestic shipments
- bridges and tunnels
• instrumentalities of transportation and communications
• personal property floater risks
• commercial property floater risks

Personal Floaters

Written on an all risk or open perils basis. A floater is coverage on property that moves from one location to another. Most personal floaters limit the insured’s settlement to actual cash value at the time of loss or the cost to repair or replace the property in question. The following perils are excluded from coverage;

• wear and tear from ordinary use
• war
• mysterious disappearance
• loss of market due to delay in delivery
• flood
• earthquake
• dishonesty of employees

In order to form a policy, the following floaters must be attached to the personal inland marine floater;

1. **Personal Property Floater: (PPF)** This policy covers all of the insured’s unscheduled personal property, worldwide on an all risk basis. Specific or scheduled items of personal property can be covered on an endorsement basis.

2. **Personal Articles Floater: (PAF)** This covers all risk protection from physical loss or damage on certain specified classes of property. This is a separate policy but it is similar to the scheduled personal property endorsement that is added to homeowners policies. Typical property which may be insured under Personal Articles Floater include: Fine arts, Jewelry, furs, cameras, musical instruments, silverware, golf equipment, binoculars, microscopes, personal furs, stamp collection, coin collection and any other item valued at $100 or more. An appraisal is necessary before the article is insured which must contain a detailed description and a value of the property.

3. **Personal Effects Floater: (PEF)** This policy is for individuals who want to have unscheduled all risk coverage for their belongings while traveling or on vacation. The policy is designed only for property that is normally carried by travelers. There is no coverage when the property is being stored, is in the home, or when the insured is not traveling. A policy can be pur-
chased for each trip, or be a permanent form of insurance for the who travels constantly. Excluded from coverage are such things as automobiles, bicycles, motorcycles, boats, securities, money, tickets, passports and valuable papers.

**Commercial Floaters**

These floaters can be written on a scheduled or blanket basis for named perils or all risk of loss. There are numerous commercial floaters designed for every conceivable segment of the business market. Examples of some commercial floaters would include;

- Physicians and Surgeons Equipment (medical equipment)
- Radium
- Salesperson’s samples
- Installation risk (individual business’ interest in the property it owns and intends to install for purchase)
- Contractor’s equipment (off the road heavy equipment)
- Accounts receivable (inability from collecting debts)
- Electronic data processing (businesses owning, renting or leasing data processing equipment)

**Bailees**

These are individuals who have temporary custody of the property of others for the purpose of performing some types of service to the property such as repairing, cleaning etc.

Some commercial property floaters are designed to cover the liability of bailees while holding the property of others such as a Jeweler’s Block Policy, Furrier’s Customers Policy and Bailees’ Customers Policy.

**Transportation Insurance**

These policies insure individuals with insurable interests in goods shipped by rail, air or land. Policies are designed for the owner of the goods in question as well as the individuals who ship them.

**Flood Insurance**

Neither personal nor commercial lines property contracts protect insureds against flood damage. The National Flood Insurance Program (NFIP) is a federal program enabling property owners to purchase flood insurance in return for their community’s adherence to a flood plan.
Any owner of property in an approved community is eligible for flood insurance. A building and its contents, residential and commercial may be insured under the Flood Program with the following exceptions:

- livestock
- roads
- gas and liquid storage tanks
- wharves, piers and bulkheads
- growing crops
- motor vehicles

In the event of loss, the insured must notify his agent who will then notify the NFIP.

**National Flood Insurance** sponsored by the Federal Government, by way of the National Flood Insurance Act of 1968, offers flood insurance to homeowners and businesses. Flood losses are generally **EXCLUDED from most policies**. The plan is only available to those persons who live in communities which have met the plan requirements and have instituted land use and water control measures. The communities must provide these improvements before their inhabitants can buy insurance. A flood is described as a temporary, partial or complete inundation of normally dry land areas by either an overflow of inland or tidal waters, an unusual and rapid accumulation or runoff of surface waters, mudslides and mudflows.

Flood insurance has a $500 deductible and there are two plans available, Basic and Regular.

**Watercraft Insurance**

Since a homeowner policy offers only small protection against the loss of the watercraft, a separate policy package is necessary. Important points to remember are property and liability protections are needed by the insured, limited property and liability coverages are available under the Homeowners Program; more, under the Boat-owners Policy; most, under the Yacht Policy. There are three types available which are based on need:

1. **Outboard Motor and Boat Insurance**: This covers the physical damage exposure to boats. This policy is written under the all risk inland marine floaters.
2. **Watercraft Package Policies:** This combines property, liability and medical payment coverage on an All Risk Basis. This is also known as a boatowner policy.

3. **Yacht Policy:** This is Ocean Marine Insurance and is usually written as a business policy because of the general use of yachts in business. The policy is designed to insure yachts, sailboats and inboard motor boats used solely for private pleasure purposes. Coverage is written on an all risk or named perils basis. The two basic coverages are;

- Damage to the hull (physical loss) collision liability insurance is included for the damage done upon a collision.

- Protection and indemnity which protects against bodily injury and property damage not otherwise covered under the damage to the hull policy.
Casualty Insurance Definitions and Terms

Overview

Casualty insurance coverage is designed to address the liability of individuals and organizations resulting from negligent acts in their personal or professional roles. The five major areas of casualty insurance are:

- general liability
- automobile
- workers compensation
- crime insurance
- bonds

Definitions and Concepts

Personal Liability: An individual is liable for injury to another. In order to collect, an injured party sues an offending party for a civil action known as a “tort”

Negligence: The law imposes a duty on everyone to act in a reasonable and prudent manner. Negligence can be seen as an unreasonable or imprudent act. However, it is never an intentional act. There are four elements of negligence;

1. the existence of a duty to act in a certain way
2. a failure to live up to that duty
3. an actual injury must occur
4. the failure in duty must be the proximate cause of the injury

Example: You own a restaurant in Oakbrook. On a dark and stormy night ten of your customers develop stomach spasms which appeared were a result of your famous “Oakbrook Stew”. As the owner of the restaurant you had an obligation to provide your customers with a safe place to eat including the food preparation. It appeared that the ceiling in the kitchen was pealing and pieces of lead infested chips fell into the stew. Well, so far you recognize that you had a duty to act in a certain way (protect customers from any possible injuries) and you failed to live up to that duty (failed to discover the contaminated stew). For the third part of negligence, those ten customers ended up in a hospital for treatment so they were injured. Finally, the fourth element was proximate cause. This is defined as an uninterrupted chain of events that can be determined to be the immediate or actual cause of a loss. Well, that certainly fits what happened at your restaurant. Fi-
nally, there has to be some demand and proof of damages. The two types of damages are;

**Compensatory (general and/or special)**

*General damages* are awarded to compensate an individual for the nonmonetary losses or inconveniences that resulted from an accident.

*Special damages* are the actual out of pocket bills incurred by an individual as a result of an accident.

**Punitive Damages**

These may be charged against a defendant who has committed an outrageous act in the eyes of the law and needs to be punished

Note: In our restaurant example compensatory damages would probably be rewarded but certainly not punitive damages unless it could be proven that you intentionally caused injuries to your customers.

**Statutory Law:** This is the law which is written by legislative bodies either on a federal, state or local basis.

**Assumption of Risk:** A party knew of an existing risk and understood an injury was possible, yet subjected to him/her self to the risk anyway.

**Absolute Liability:** An individual can be held liable for injury, even if there was no negligence involved. This is liability without fault known as *strict liability*.

**Statutes of Limitation:** These are time frames set forth by statutory law, during which an injured party can bring a lawsuit. Unless legal action is brought within this time period the right to sue for injury will disappear.

**Common Liability Exposures:**

- *premises*: Every piece of property has a premises exposure because of the many persons who visit a premises on any given day - i.e. a customer visiting your store or the mail person delivering mail.

- *operations*: Businesses have on and off-premises activities such as with customers, delivery persons etc.
• **Products:** Manufacturers, wholesalers and retailers are legally liable for bodily injury or property damage caused by the products under their control at their premises as well as for injury arising out of the use or consumption of merchandise away from the premises of the manufacturer or vendor.

• **Completed Operations:** This exposure is very similar to the products exposure as it involves possible liability for work that has been performed for another. (i.e. contractor installs a vaulted ceiling in your study room and after he leaves the ceiling falls on your head)

• **Contracts:** Contracts which are deemed necessary and basic to the conduct of business are covered automatically under premises-operations liability coverage. Contractual liability coverage does not protect the insured for legal liability arising out of a breach of contract. These contracts are called “incidental contracts” or “insured contracts” and include:
  - lease of premises agreements L
  - easement agreements E
  - agreements to indemnify municipalities A
  - sidetrack agreements S
  - elevator maintenance contracts E

• **Lease:** The lease details the agreement for one wishing to rent space in another's building.

• **Easement:** This is an agreement by which the owner of land allows another party to use the land in a limited way.

• **Municipalities** often require local businesses to indemnify or protect them from the possible consequences of a particular act such as a sidewalk sale.

• **Contingent Liability:** This refers to liability which arises out of the work done by independent contractors. In general, an individual business cannot be held responsible for the negligence of an independent contractor other than the following exceptions;
  - the activity is legal
  - a situation is involved which does not permit delegation of authority
  - the work is inherently dangerous
• **Personal Injury:** This is an injury, other than a bodily injury, arising out of one or more of the following actions:

  ◊ false arrest, detention or imprisonment
  ◊ malicious prosecution
  ◊ wrongful eviction
  ◊ slander or libel
  ◊ violation of right of privacy

• **False Imprisonment:** This is the unlawful detention of a person depriving the individual of his/her personal liberty.

• **Malicious Prosecution:** This is when one party accuses another of starting a prosecution maliciously against this first party without probable cause that the action would succeed. The required three elements are as follows;

  ◊ a criminal or civil suit must have preceded it
  ◊ this suit was started out of malice by one individual against another
  ◊ the decision of the first suit must have been favorable to the defendant in that case

• **Wrongful Eviction:** This usually involves the physical eviction of an individual from a public place in violation of his/her civil rights.

• **Defamation:** The act of holding up a person to ridicule, scorn or contempt to a respectable and considerable part of the community by spreading untruths. Libel is in writing and slander is spoken.

• **Invasion of Privacy:** Basically the right to be left alone.
6 Commercial General Liability Policy

Overview

This is liability insurance for most types of commercial or business exposures. The Commercial General Liability Policy is part of the Commercial Package Policy and can be sold in conjunction with other coverages or can be purchased independently. There are many different coverages available under the CGL policy, each designed for a particular type of exposure. Under a CGL policy the named insured, spouse, partners, officers, directors and shareholders, and SPOUSES if acting within the scope of business as well as employees, managers or anyone acting with authority within the business can be covered.

Coverage Triggers

Occurrence means an accident, including continuous or repeated exposure to substantially the same general harmful conditions. This requires notification promptly when a situation occurs which may lead to liability. Covers Injury or Damage done during the policy period.

Claims Made requires the insured to notify the company as soon as practical which must include the nature and location of any injury or any damages which arose from the occurrence. Covers claims made during a policy period.

Covered Territory includes all parts of the world if the injury or damage basically arises out of goods or activities of a person whose home base is in the United States, its territories and possessions.

Claims

A claim by a person or organization seeking damages will be deemed to have been made when notice of such claim is first received and recorded by any insured or the insurer.

Coverages

The Commercial General Liability Policy provides the following three coverages on an occurrence or claims made basis;

- Coverage A - Bodily Injury (BI) and Property Damage (PD) Liability
- Coverage B - Personal and Advertising Injury Liability
• Coverage C - Medical Payments

**Coverage A: BI and PD Liability, Coverage B and C**

**Coverage A**

Coverage A is for bodily injury and property damage liability. This includes premises and operations liability, products and completed operation liability, contractual liability.

Property damage means physical injury to tangible property, including resulting loss of use of that property as well as loss of use of tangible property that is not physically injured.

Under Coverage A the company will pay any sums that the insured becomes obligated to pay because of BI and PD. Liability exposures covered under A include:

- premises and operations
- products and completed operations
- contractual liability for insured contracts (incidental contracts)

Other liability exposures such as fire legal liability, nonowned watercraft are also covered. The policy will pay those sums that the insured becomes legally obligated to pay as damages because of bodily injury or property damage to which the insurance applies. The insurer has the right and duty to defend any suit seeking those damages.

**Exclusions**

Coverage A does not apply to BI and PD caused by;

- expected or intentional acts
- work related
- automobile, aircraft or watercraft activities
- dram shop (liquor liability)
- personal property of others in the insured's care
- discharge of pollutants
- war
- assumption of liability by contract
- transportation or use of mobile equipment
- property damage to the insured's product or work
- property damage to impaired property
- loss, cost or expense incurred by the insured for the recall of a product because of a known or suspected defect
Coverage B - Personal and Advertising Injury Liability

This coverage will pay those sums which the insured is legally obligated to pay for damages, due to personal injury or advertising injury. Coverage applies to personal injury if it arises out of the conduct of the insured's business. Personal injuries are not covered if they result from the insured's personal life.

Personal Injury includes malicious prosecution, libel, slander, false arrest, defamation of character, unlawful eviction or entry and violation of the right to privacy.

Advertising mistakes can result in exposure to vast sums of liability due to improper advertising. An injury which can be labeled an advertising injury is one which is created due to one or more of the following:

- stealing the advertising ideas or style of another
- copyright, title or slogan infringement
- written or oral publication material violating a person's privacy rights
- oral or written publication leading to slander or libel of a person or of his/her organization's goods, products or services.

Coverage B Exclusions

When the insured;
- knows the oral or written publication is false
- has published material which is the focus of a personal injury claim before the inception of the policy
- willfully violates the law
- assumes liability in a contract or agreement

Not covered if the injuries results from;
- a breach of contract
- the failure of goods to conform to advertised quality
- the wrong description of the price of goods, products or services
- an offense committed by an insured whose business is advertising, broadcasting, publishing or telecasting

Coverage C

The coverage agrees to pay medical expenses which are incurred within one year of an accident during a policy period when bodily injury occurs on the premises owned or rented by the insured, or for bodily injury which results from the insured's operations.
Negligence does not have to be established in order to make a policy pay a claim. It is no fault coverage with no reimbursement for medical payments for necessary hospital, ambulance, funeral expenses, professional nursing care, first aid which is given when an accident occurs, any necessary medical, surgical, prosthetic devices, x-ray and dental services.

**Exclusions**

**Medical payments will not cover expenses for bodily injury to:**

- insureds
- persons hired to work for the insured or a tenant of an insured
- tenants of the insured
- persons entitled to workers compensation
- persons involved in an athletic event
- persons injured resulting from the products-completed operations hazard
- persons excluded under Coverage A
- persons due to war

**Supplementary Payments**

Under Coverage A and B the insurance company will also pay the following:

- all reasonable expenses and up to $100 per day of lost wages when the insured is incurring expenses at the insurer’s request to help in an investigation or defense of a claim or lawsuit.
- up to $250 for cost of bail bonds required because of accidents or traffic law violations arising out of the use of any vehicle to which the bodily injury liability coverage applies. The insurer does not have to furnish these bonds.
- any expenses incurred by the insurance company
- all costs levied against an insured in a lawsuit
- reasonable expenses insured in defense of a claim
- interest payments, both pre-judgement and post judgement

**Insureds** include individuals, partnerships and other organizations which may be insured under the CGL. Employees of these insureds acting within the scope of their employment are also covered. The insured’s legal representative is considered an insured if the insured dies, but only with respect to duties as the legal representative.

**Limits of Insurance** are shown in the Declarations with the limits defined below;
Aggregate Limits of liability are established for all coverages to include two sets: The first set is for products-completed operations claims and the second for all other coverages.

General Aggregate Limit is the most the insurance company will pay during the policy period for BI and PD except those provided for under Products-Completed Operations coverage.

Personal and Advertising Injury Limit is a per person or organization limit. The amount shown is the most the company will pay for the sum of all personal and advertising injuries to one person or organization.

Each Occurrence Limit is the most the insurance company will pay for any one occurrence, subject to the General Aggregate.

Fire Damage Limit is a per fire limit.

Medical Payments Limit is a per person limit.

Conditions found in both the occurrence and claims made forms

Bankruptcy condition states that if the insured becomes bankrupt or insolvent the insurer cannot refuse to pay claims that may be covered under this policy.

Duties in the event of occurrence, claim or suit requires that the insured promptly notify the insurance company of an occurrence that may result in a claim or suit and give written notice to the insurer of any claim that has been made or suit that has been brought against the insured.

Legal action against us states that no person or organization has the right to join the insurance company as a party or bring the insurance company into a suit.

Other Insurance condition states that if the insured carries more than one CGL policy, coverage A and B will be effected as follows;

- **primary insurance**: if the policy were written with the intent that it respond to a claim first, it will do so, until its limits of insurance are exhausted. Another primary policy will pay its share in accordance to the method of sharing provision described in the policy.
• **excess insurance**: this policy will respond after other policies have responded and exhausted their limits of insurance.

• **method of sharing insurance**: this policy will pay its portion of the loss.

**Premium Audit** is computed by the insurer. Premium shown as advance premium is a deposit premium only. At the close of each audit period the insurer will compute the earned premium for that period. Audit premiums are due and payable on notice to the first named insured. Excess premium will be returned by the insurer if the sum of the advance and audit premiums is greater than the earned premium.

**Defense Costs** incurred by the insurer in defending a suit is a very important benefit. Settlement of a case prior to suit is seen as a preferable course of action to all concerned for the following reasons;

- the illogical basis for many court settlements
- the costly and lengthy nature of litigation for both sides
- the changing strength of a case based on tie
- legal fees mount up quickly

**Other Liability Coverages**

These specialized coverage forms may be added to the Commercial General Liability Forms.

**Owners and Contractors Protective (O&CP)**

This policy has been designed to cover an insured’s independent contractor exposure. It provides liability protection in those situations where the law holds the owner or principal contractor liable for the negligence of an independent contractor, especially when the work is unlawful, very dangerous and such that the liability for it cannot be transferred or delegated. Bottom line, the O&CP is designed to cover one liability exposure and one liability exposure only: the independent contractor or contingent liability exposure. All other liability exposures are excluded from coverage.

Claims will be paid according to the insuring agreement under O&CP insurance for bodily injury or property damage due to operations which are performed for an insured who is named by a contractor (as designated in the declarations agreement and only at the designated location). This policy will also help pay for defending a lawsuit.
Professional Liability

Professional liability arises from a failure to use due care and the degree of skill required and expected in a particular profession. A profession is a vocation, calling or occupation involving labor, skill, education and special knowledge of an intellectual nature. As an example, hospitals can be sued for unauthorized release of information; doctors can be sued by injured patients; attorneys can be sued for giving bad advice, etc.

Typical professionals include physicians, attorneys, accountants, engineers, architects, securities and insurance professionals.

The two broad types of professional liability insurance is malpractice and errors and omissions.

Malpractice insurance addresses the professional liability needs of the medical and allied professions. There are specific malpractice policies for physicians, surgeons, dentist, hospitals, druggists, nurses, opticians etc.

Errors and Omissions insurance addresses the professional liability needs of lawyers, engineers, architects, insurance agents, real estate agents, registered representatives etc.

Both of these are limited policies. In order to have a full range of liability protection it would be necessary to purchase some other general liability policy.

Examples of specific professional liability policies:

- Physicians, Surgeons and Dentists
- Partnership
- Hospital
- Lawyers
- Insurance agents and brokers
- Directors and Officers - Although generally excluded from other types of liability coverage, this coverage will cover their decisions, action and/or inaction.

Umbrella Liability Coverage

These policies are designed to protect an insured individual or business agent against catastrophic or disastrous claims. This type of policy provides coverage over and above or an excess of primary coverage. The umbrella usually provides coverage in some dollar amount,
normally at least a million dollars over and above the primary amount carried. The purpose of an umbrella liability policy is to provide low cost coverage due to exposure of businesses because of a greater variety of liability hazards.

In recent years, umbrella liability policies have become quite popular with professionals and members of middle and upper management for their business and personal liability exposures.

Remember, primary insurance pays first, up to the policy limits, regardless of other insurance in effect. Excess insurance, like an umbrella policy, begins to pay after primary insurance has been exhausted.

**Personal Umbrella Coverage**

This type of insurance policy provides individuals and families with high limit/excess protection over basic Comprehensive Personal Liability (Section II of the Homeowners Policy), automobile liability and other liability insurance carried with respect to property of a personal/family nature, as distinguished from business and professional activities and property. Personal Umbrella Liability insurance is written with a minimum limit of liability of $1 million with higher limits available.

**Commercial Umbrella Coverage**

This policy provides excess general liability, automobile liability, employers liability limits and also protects the insured firm from exclusions and gaps in the primary liability policies which serve as underlying insurance.

**Additional Review Notes:**

- Any CPP policy must have AT LEAST: Declarations page, Conditions section and General Coverage Part or Form (which describes the coverages)

- **Stacking of liability claims** occur when an occurrence happens over a 2-3 year period. Each years limit could be stacked up to provide larger liability limits. A **Claims Made Policy** is designed to prevent this from happening.
7 Automobile Insurance Policies

Automobile Insurance Liability & Medical Payments

Automobile liability addresses third party claims for bodily injury and property damage arising out of the insured’s negligent operation of an automobile. In Illinois, motorists are required to have some minimum levels of coverage set forth by state statutes. The basic coverage provided by automobile policies includes liability, medical payments, physical damage, and uninsured motorist protection.

Personal Auto Policy (PAP)

PAP is designed for personal auto exposure, not commercial. Eligible vehicles for PAP coverage include any private passenger auto and any pickup or van with a gross weight less than 10,000 pounds which is not used in a freight or delivery business. Also included are vehicles which are leased for a minimum period of six consecutive months.

The insured for contractual purposes referred to as “you” and “your” throughout the policy is considered to be the insured named in the Declarations and/or his/her spouse.

Coverages

Part A - Liability Coverage

This coverage provides payment for Bodily Injury and Property Damage resulting from the insured’s use of an automobile for which the insured becomes legally liable. The day in which coverage begins under a PAP policy is at 12:01 a.m. on the date listed in the policy. Under this Part, the company promises to settle and defend claims brought against the insured involving the insured’s use of an auto. The company also agrees to pay for all defense costs.

The definition of insured is quite broad and includes not only family, but anyone you give permission to drive your vehicle. The liability coverage under a PAP policy is for any insured who becomes legally responsible for the bodily injury or property damage to someone else because of an auto accident. An insurance company will pay sums up to limits stated in the declaration portion of the PAP.
The PAP is not available to corporations, partnerships or other organizations that can be incidentally responsible for the use of insured vehicles.

Damages paid for **bodily injury** include not just the payments of actual medical costs which can be documented, but also for a person’s pain and suffering due to the injury. **Property damage** extends to any kind of property which is damaged due to the negligent operation of an auto including vehicles, buildings, street lights or any other kind of stationary object.

The insurer has the option to settle or defend any claim or suit which it deems appropriate. The insured cannot dictate coverage payment or refusal.

**Liability Limits**

The PAP is written on a **single limit basis**, one amount representing the aggregate limit for all claims arising from any one accident. If a policy is written for $100,000 then it would cover all claims arising out of one accident regardless the number of insureds, claims made or vehicles involved.

In contrast, some auto policies are written on a **split limit basis** for liability coverage such as **20/30/15**. The first two numbers are related to bodily injury. In this case, $20,000 is available as a maximum in any one accident for any one person; $30,000 as a maximum for all persons in any one accident; and $15,000 as a maximum for all property damaged in any one accident.

**Part A-Insureds - Who Are They?**

- the insured or any family member
- any person using your vehicle with permission
- any organization with respect to legal responsibility for acts or omissions of a person for whom coverage is afforded under this part.
- Bottom line, coverage follows the auto

**PAP Example:**

*Melvin Doofis, a citizen of a town called Eat n Plenty, is the head coach of the town’s football team. On a hot summer night Melvin decides to have a outdoor pool party at his house for the entire football team, friends and relatives. As all of the 250 guests brought automobiles to the dinner, parking was a problem. In*
Melvin’s driveway was Melvin’s car, parked at the top of the driveway while Billy Bob, his quarterback, parked his car just to the right side of Melvins. In back of those cars were two cars belonging to the Eat n Plenty cheerleaders, Pattie and Matilda.

In the middle of the party Melvin ran out of Coors beer. Without more beer the team was getting rather hostile and ugly. Melvin who wasn’t drinking chose Herman, another non-drinker to go with him to purchase more beer.

Melvin borrows Matilda’s car which is located in the driveway nearest to the street. Matilda carries minimum limits of 10/20/5 liability insurance. Melvin carries 200/300/200.

Let's take a look at the following set of facts to help you understand some of the issues we have presented and discussed:

1. Whose auto insurance liability applies if there is an accident? Matilda’s liability insurance applies when Melvin drives Matilda’s car. Melvin becomes an insured, by definition under Matilda’s liability coverage.

2. If Melvin negligently runs a stop sign, hits a light pole and sustains injuries to himself and causes injuries to Herman, whose liability insurance would cover both Herman’s and Melvin’s injuries? If Melvin negligently hits a light pole as described, Matilda’s liability insurance would apply to Herman’s injuries because Melvin is an insured, by definition, under Matilda’s policy. Neither liability insurance policy would apply to Melvin’s injuries: Melvin is an insured under Matilda’s policy: Melvin’s personal policy doesn’t apply to Matilda, the insured.

3. If Herman sustains a serious injury resulting in a $80,000 claim, Matilda’s auto liability coverage would apply on a primary basis for $10,000 to Herman’s injuries. In turn, Melvin’s auto liability coverage (on his own car) would pay the remaining $70,000 on an excess basis.

Remember, a primary coverage must be exhausted first before an excess coverage begins.

Supplementary Payments

- up to $50 a day for lost wages when the insured is required to attend a legal hearing or trial
- bail bonds costs up to $250
• cost of bonds to release attachments in any suit the company defends
• any expenses incurred by the insurance company
• reasonable expenses incurred at the insurer’s request
• interest payments (post judgment)

Exclusions

• insured intentionally causes bodily injury or property damage
• for damage to property owned or being transported by that person
• for damage to property rented to, used by or in the care of that person.
• for bodily injury to an employee of that person during the course of employment. This exclusion does not apply to bodily injury to a domestic employee unless workers compensation are required or available for that domestic employee.
• people engaged in the business or selling, repairing, serving, storing or parking automobiles
• any vehicle which is being used for regular business purposes
• any liability arising out of the ownership or operation of a vehicle while it is being used to carry people or property for money or a fee

Out of State Coverage

If the insured becomes involved in an auto accident out of state and the state involved requires higher liability limits than the insured maintains, the PAP will provide the higher specified limit for this accident.

Part B - Medical Payments

Regardless of fault, the insured, his family and passengers are covered for necessary medical and funeral expenses sustained within 3 years from the date of accident. The insured and family members are also covered if they are struck by an auto when they are a pedestrian.

This coverage is a single limit of anywhere from $1,000 up to $10,000 and it applies to a single person per accident.

If there is other applicable auto medical payments insurance, the policy will pay only its share of the loss. The insurer’s share is the proportion that this policy’s limit of liability bears to the total of all applicable limits.

Exclusions - does not apply to any persons for bodily injury;

• sustained while occupying any motorized vehicle having fewer than four wheels
• covered autos used as a livery conveyance
• vehicles used for residential living
• used during the course of employment if workers compensation is available for the bodily injury
• any auto other than a covered auto owned by or used regularly by a named insured or family member.

**Part C - Uninsured Motorist Coverage**

An uninsured motorist is someone that may strike you, but who does not carry insurance, including hit and run drivers. So, Part C agrees to pay damages which an insured is legally entitled to recover from the owner or operator of an uninsured vehicle because of bodily injury sustained in an auto accident.

In Illinois, uninsured motorist (UM) coverage is mandatory, 20/40 limits and must be purchased by every motorist. The uninsured motorist coverage pays for amounts that cannot be collected because the other driver did not have enough insurance, does not have enough assets or is not covered by insurance. If the insurer and insured do not agree on whether or not a UM claim is covered or, if covered, for how much, either party may demand arbitration.

**Underinsured Motorist Coverage**

This is available by endorsement under the PAP, covers the insured when involved in an accident with a driver who has auto liability insurance, but the limit of this insurance is insufficient to pay for the insured's damage.

Underinsured motorist coverage pays bodily injury coverage caused by the operation of motor vehicles which are underinsured. The underinsured motorist coverage allows a covered person to be paid the difference between what actual damages for bodily injury were and what the limit of the other drivers insurance was when it was not sufficient to pay the entire claim of the injured party.

**Part D - Coverage For Damage To Your Auto**

This coverage is divided into two separate coverages;

• collision
• comprehensive

**Collision** means the upset of a covered auto or its impact with another vehicle or object. When a loss is not considered to be from a collision it will fall under other than collision coverage. Autos will be replaced on an ACV basis.
Comprehensive coverage is a loss other than from collision and addresses damage losses to the insured vehicle caused by;

- missiles or falling objects
- theft or larceny
- explosion or earthquake
- windstorm
- hail, water or flood
- malicious mischief or vandalism
- riot or civil commotion
- contact with bird or animal
- breakage of glass

Exceptions;
- carrying people or property for a fee
- electrical breakdown
- mechanical breakdown
- normal wear and tear
- road damage to tires
- damage to radar detection equipment
- loss of any CB radio, TV monitors, computers etc.
- custom furnishing in any pickup or van

Transportation Expense

Under Part D the insurer will pay up to $15 per day, to a maximum of $450, for transportation expenses incurred by the insured. This applies only in the event of the total theft of your covered auto. Towing coverage may also be available.

Rental Cars

Car rental companies place the responsibilities for loss or damage to the rental car itself upon the renter. Collision damage waivers may be purchased to relieve the renter of all or part of his/her responsibility for loss or damage to the car. It should be noted that under a PAP, Coverage D will provide some coverage for the rental car.

Cancellation

Once a policy has been in existence for period of 60 days the policy cannot be canceled unless for nonpayment of premiums, suspension or revocation of a drivers license or if the policy was obtained through material misrepresentation.
Nonrenewal

If a company decides not to renew a policy it must mail a notice to the insured at least 20 days before the end of the policy period.

Part E - Duties of the insured after a loss

- Notify the police
- Notify the company
- Be specific as to all the details of the loss, including when and where the loss occurred, how it occurred, names and addresses of witnesses and data about injured persons
- Provide access to any information needed
- Submit a completed proof of loss form
- Protect the auto from further damage
- Allow the company to inspect and/or appraise any damage.

Commercial Auto Insurance

Commercial Auto Insurance is designed to address commercial automobile risk exposures. Depending on the nature of the exposure, one of the following is basic to the development of a Commercial Auto Coverage Part;

- Business Auto Coverage Form
- Garage Coverage Form
- Truckers Coverage Form

Business Auto Policy (BAP)

The business or commercial auto policy is for owners of commercial vehicles such as sole proprietors, partners, corporations etc. BAP is similar to PAP in that it provides liability coverage and physical damage coverage. Insured parties under a BAP include the named insured person or organization for the covered auto, and anyone using the auto within the scope of permission given. This policy is designed to cover all commercial automobile exposures, other than those which are better handled by the Truckers or Garage policies.

The liability coverage will pay all sums an insured legally must pay as damages because of bodily injury or property damage to which the insurance applies, caused by an accident and resulting from the ownership, maintenance or use of a covered auto.
**Comprehensive coverage** applies to loss from any cause except collision or overturn while **collision** coverage applies to loss caused by collision with another object or overturn.

**Garage Coverage Form**

This Form is for automobile type businesses such as gas stations, parking garages and auto dealers who cannot get a BAP. It is a unique form of coverage because it covers both auto and business liability. Coverage is provided for autos in the insured’s care, custody and control, coverage that is specifically excluded in other commercial auto coverages.

**Truckers Policy**

A trucker is defined as any person or organization engaged in the business of transporting property by auto for hire. This policy is geared to meet the specialized needs of persons and organizations involved in the trucking industry. Truckers policy provides the same coverages as the BAP, but adds a trailer interchange coverage which provides that the insurer will pay the sums the named insured legally must pay as damages for loss to an unowned trailer or its equipment. A trailer interchange agreement is a written agreement which requires one trucker to reimburse the other for any damage to the other’s owned trailer while in his/her possession.
8 Other Insurance Policies

Workers Compensation Insurance

This insurance covers those people who are injured, become disabled or die from injuries or illness arising out of and occurring in their course of employment and have a right to hold employers liable for economic or financial damages under workers compensation laws.

The employee does not have to prove fault as an employer cannot defend against the action at all unless he/she can show that the employee was inured or suffered an injury or died due to willful negligence. Willful negligence is defined as a deliberate act or failure to act with requisite indifference, or if the employee is intoxicated.

Compulsory laws require specified benefits be provided by employers covered under the law while Elective workers compensation, which Illinois prescribes to, states that employer or employee may elect not to be covered under certain conditions as prescribed by state statutes.

It should be noted that none of the state workers compensation law covers every employer and/or type of employment. The workers compensation and employees liability policy provides coverage for payments which are required under state workers compensation law as well as the liability risk for injuries and diseases which are occupationally related.

The following types of employment are not covered under state workers compensation laws because of their temporary status;

- farm labor
- domestic employment
- employees of religious, charitable and nonprofit educational institutions
- casual employees

Ways to Meet Obligations

- self insurance
- private insurance
- state funds

Self insured means a business organization that chooses to retain the exposure of workers compensation rather than purchase a workers compensation policy. In most states an employer can retain the
workers compensation risk if they show evidence of financial ade-
quacy. Retention or self insurance is designed only for large employ-
ers. They do so by meeting certain criteria such as;

- posting a surety bond which will guarantee the security of
  benefit payments
- showing evidence of the ability to administer the benefit pay-
  ments and other workers compensation services that may be
  mandated by their state laws.

Part I - Workers Compensation Insurance

This part applies to bodily injury caused by accident or disease. Pay-
ments are made to employees regardless of fault as long as the inju-
ries are work related.

Part II - Employers Liability Insurance

This applies to bodily injury by accident or bodily injury by disease.
Bodily injury includes resulting death. Under this part, the policy pays
for damages resulting from bodily injury claims initiated by employees.
This coverage protects the insured employer from negligence suits
brought by employees because of work related injuries.

Work related vs. Non-work related

To be covered under Workers Compensation, an injury or disease
must arise out of and in the course of employment. The employee
must have been engaged in work related activities. A non-work
related injury is one suffered by the employee while not in the
course of employment. As an example, the insured sponsors an
employee picnic. During the festivities an employee is injured
playing softball. This is a non-work related injury and would not
be covered by workers compensation.

Part III - Other States Insurance

An optional coverage which automatically provides coverage to the in-
sured in other states as long as those states are specified and the in-
sured informs the company about such additional states as soon as
work begins. It is not available in those states that have a state fund
in which private insurance is not allowed. This protection is important
for employers with expanding interstate operations.
Part IV - Your Duties If Injury Occurs

If an injury occurs to a covered employee, the employer must notify the insurance company immediately and the insured must cooperate with the insurer and promptly notify the company of an employee’s injury. The insurer reserves the right to inspect the workplace at anytime. The insured can cancel at any time while the insurer must supply 10 days notice of cancellation.

Miscellaneous Workers Compensation Points

- Employees come under the provision of workers compensation laws while independent contractors are not covered.

- Workers compensation benefits are payable regardless of fault.

- Basic rates are based upon a system of job classifications and manual rates. The premium basis itself is the payroll and basic premiums are determined by multiplying the manual rate for each code by every $100 of payroll for that classification.

- While smaller employers usually pay manual rates, very large employers enjoy experience rating which incorporates premium adjustments based upon actual loss experience.

- Benefits payable are generally restricted to the following;

  ◊ Medical benefits - unlimited coverage relating to covered expenses. No dollar or time limits!
  ◊ Disability income benefits which is normally based on earned wages as well as the duration and severity of the injury. The rate of wages provided under workers compensation laws differ from state to state but the benefit is usually set at some percentage of the employee’s wage. Partial disability available as a percentage of lost wages are restored.
  ◊ Survivor death benefits are generally lump sum payments paid to survivors. The burial allowance maximum is $1,700. Deceased workers wages are paid at the rate of 66 2/3% to a surviving spouse/children up to a maximum of $250,000 or weekly payments for 20 years of the total temporary disability rate – whichever is greater. Children remain eligible for benefits until age 18 or up to age 25 if still in school.
  ◊ Rehabilitation benefits are costs associated with physical therapy to regain the use of injured body parts. Physical, mental and vocational rehabilitation including maintenance costs, incidental expenses and any required institutional care.
• A second injury fund helps pay increased compensation which is required because an employee has one injury and then is later injured again

Crime and Bonding

Money and valuables are burglarized from premises or robbed at gunpoint or stolen by employees. Let’s review some of the basic definitions;

• **Theft** is any act of stealing and includes the acts of burglary and robbery.

• **Burglary** is the forcible entry or exit into or out of an insureds locked premises and the carrying away of property belonging to the insured. Burglary can also include forcing a guard to open a locked premises.

• **Robbery** is the forcible removal of an insured’s property due to fear or threat of violence or means of injuring or murdering a messenger or custodian. A **messenger** is defined as an insured, partner, officer or any other employee of the insured authorized to have custody of the insured property outside the insured premises. A **custodian** can be defined in the same way as a messenger inside the premises. A **guard or watchperson** means any person the insured retains specifically to have care and custody of property inside the premises and who had not other duties.

• **Premises Burglary** (Coverage Form E) covers all property for loss inside the premises other than money and securities, except motor vehicles, trailers and semitrailers, and equipment and accessories attached to them. Physical damage to the premises as demonstrated by forcible entry due to tools, electricity, explosive, and chemicals must be shown. Evidence of visible signs of the forced entry must be present prior to recovery for the loss. Robbery of a watchman is also covered.

• **Safe Burglary** is the felonious removal from within a safe or a vault items which are not money or securities. Robbery is covered both inside and outside the insured premises. In order for safe or vault coverage to apply there must be evidence of robbery or violence with tools or explosives. Even if the entire safe is removed from the physical location, coverage will apply. Items such as cash registers or key lock safes are not considered to be safes but the coverage can be added for them by endorsement.
• **Robbery and Safe Burglary** (Coverage D) makes provision for coverage inside the premises and outside the premises of property other than money and securities, which can be covered by endorsement. Inside the premises coverage may be written to cover both robbery and safe burglary or can be limited to either robbery or safe burglary. Outside the premises coverage applies to robbery of property in the care and custody of a messenger.

◊ **Robbery and Safe Burglary - Money and Securities** (Coverage Form Q) covers money and securities inside the insured premises while in the care of a custodian as well as inside the insured premises or banking premises while in a safe or vault against robbery and safe burglary. Furthermore, property other than money and securities is covered outside the insured premises while in the care of a messenger against robbery.

• **Theft, Disappearance and Destruction** (Coverage Form C) covers only money and securities. Form C applies inside the insured’s premises or a banking premises against theft, disappearance or destruction. Provision is made for similar coverage outside the premises when money and securities are in the care and custody of a messenger.

• **Robbery of a Custodian** provides coverage to those who qualify as insureds including officers or partners of a company, or any other person who is regularly employed by a company and duly authorized by that company to have custody of insured property within a premises. Excluded from coverage would be watchman, janitors or porters.

• **Fidelity Bonds** protects an insured against the dishonest or fraudulent acts of employees. Fidelity bonds are often called dishonesty insurance. All risk coverage is not provided. Most fidelity bonds contain a discovery period which is a period of time for which indemnity still exists for loss after the bond itself has expired (usually one year).

• The individual fidelity bonds can be divided into the following classes;
  ◊ individual
  ◊ scheduled
  ◊ blanket

**Individual fidelity bond** covers one person.
Scheduled fidelity bonds can be either name schedule or position schedule. To schedule something is to list it. Fidelity bonds written on a name schedule basis would list the names of the individuals to be bonded. When written on a position schedule basis, fidelity bonds list the positions to be bonded. The amount of the bond or penalty would be listed.

Blanket fidelity bonds provide blanket protection for an employer, covering all employees without exception. As a result, if a covered loss occurs, there is no need to identify the dishonest employee; the employer need only prove that the loss occurred.

There are two types of blanket bonds;

1. **Commercial blanket bond** provides for the bond’s penalty (limit) to be the maximum amount applicable to any single loss, regardless of the number of employees involved. This has an aggregate penalty. Although a loss does not reduce coverage for any future losses caused by other employees, no more coverage will be provided for future losses caused by someone who has already has created a loss. There is a one year discovery period. There is coverage whether dishonest employees act separately or in collusion.

2. **Blanket Position Bond** provides for a specific individual penalty listed in the bond for each of the insured’s employees. This bond has a multiple penalty which means that the payment of any one loss does not reduce the coverage offered for future losses which may occur due to the actions of other employees. There is a two year discovery period.

Surety Bonds

This is the guarantee of an obligation. While fidelity bonds operate much like insurance, surety bonds adhere more strictly to the concept of suretyship; the surety lends its name and credit to guarantee an obligation made by one party (the principal) to another (the obligee).

The following represents the categories of the main surety categories;

- court
- contract
- license and permit
- public official
- federal
- miscellaneous
EXAM CERTIFICATION SECTION
Answer Sheet – IL30520 (10275)
IL Ins – 15 Hrs; CFP – 10 Hrs; CPA – 7.5 Hrs

1. PRINT your name & insurance license number where indicated. PRINT NEATLY as this is the information which will be reported to the State – illegible letters and/or numbers will result in delays.

2. ____ Check here if this is for CFP
3. ____ Check here for NASD
4. ____ Check here for Illinois insurance.

5. Indicate by which method you would like your completion notification sent; fax or mail choose one
6. Indicate fax number below if you want your results faxed. You should receive within 36 hours.
7. If we are mailing your results we will mail to the address of record. You should receive within 7 days.
8. If you are not successful we will call you. Dept of Insurance rules preclude a retake of the same exam. Another exam will be provided to you at an additional charge.
9. Fax (847/705-3837) or mail (579 N 1st Bank Dr, #210; Palatine, IL 60067) this completed answer sheet. Please save time and trees – no cover sheet is needed.

Print Name: _____________________________________________________________________
Insurance License No. (Should be SS #) ______________________________________________
Day phone #: ____________________________ Notify me by: Mail: ___ Fax: ___
Choose only one of the above
Fax number: _________________________________

I, the undersigned certify that I ALONE completed this self-study course and corresponding final exam:
Student Signature: __________________________________________________________________

Place your answers on the line next to the appropriate test question number on the right!

1. ____ 9. ____ 17. ____ 25. ____
2. ____ 10. ____ 18. ____
3. ____ 11. ____ 19. ____
4. ____ 12. ____ 20. ____
5. ____ 13. ____ 21. ____
6. ____ 14. ____ 22. ____
7. ____ 15. ____ 23. ____
8. ____ 16. ____ 24. ____
1. The purpose of insurance is to:
   A. Reduce risk
   B. Spread risk amongst others
   C. Assume risk
   D. Manage risk

2. Which of the following are types of risks?
   A. Speculative risk
   B. Pure risk
   C. Mechanical risk
   D. Both A & B

3. Property and casualty policies are written in which of the following?
   A. All of the following
   B. All risk
   C. Open perils
   D. Named perils

4. Which of the following is a loss which occurs directly through an unbroken chain of events?
   A. Direct loss
   B. Indirect loss
   C. Consequential loss
   D. None of the above

5. Which of the following are examples of someone having an insurable interest?
   A. Mortgage holder
   B. Person owning property
   C. Person living on the property
   D. All of the above

6. All of the following are legal parts of an insurance contract EXCEPT:
   A. The offer
   B. Collateral
   C. Consideration
   D. Acceptance

7. Evaluating a claim is the duty of the:
   A. Insured
   B. Judge
   C. Victim
   D. Insurer

8. Who has the initial responsibility for evaluating or field underwriting specific business?
   A. Underwriters
   B. Insurer
   C. Paramedics
   D. Insurance producers

9. Actual cost represents replacement cost less;
   A. Indemnity
   B. Value
   C. Replacement cost
   D. Depreciation

10. If the insured cancels the policy any unearned premium will be returned on what basis?
    A. Loss
    B. Pro rata
    C. Pro forma
    D. Short rate
11. A typical coinsurance clause of a property policy will state that an insured has to satisfy a level of what percent?
A. 80%
B. 65%
C. 50%
D. 25%

12. Newly acquired or constructed property is covered up to what percent per building?
A. 15%
B. 20%
C. 25%
D. 10%

13. Broad Form in commercial property insurance covers;
A. Falling objects
B. Fire
C. Lightning
D. All of the above

14. Earthquake only coverage is always available.
A. False
B. True

15. Homeowners coverage is identified as what type of forms?
A. HO
B. Home O
C. Hoo
D. Hhoo

16. Personal property losses are settled on a replacement cost basis.
A. False
B. True

17. The BOP is a;
A. Single peril policy
B. Multi peril policy
C. Double peril policy
D. All peril policy

18. Which of the following is a duty of the insured?
A. Protect the property from further damage
B. Abandon burned out property
C. Assign benefits to the mortgagee
D. Allow the company to subrogate

19. Negligence can be seen as a reasonable or imprudent act.
A. False
B. True

20. Under a CGL, personal and advertising injury liability is covered under Coverage;
A. None of the following
B. A
C. C
D. B

21. False imprisonment is the unlawful detention of a person depriving the individual of his/her personal liberty.
A. True
B. False

22. Personal injury includes;
A. Both B & C
B. Malicious prosecution
C. Libel
D. Negligence
23. **Regarding umbrella liability coverage, which insurance pays up first?**

A. Final  
B. Excess  
C. Umbrella  
D. Primary

24. **A PAP policy is always available to corporations.**

A. False  
B. True

25. **Which policy is used for business or commercial vehicles?**

A. BAP  
B. PAP  
C. CAP  
D. PAB
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