

LESSON 5.4 LIABILITY AND PHYSICAL DAMAGE COVERAGE

Today we will complete our review of the liability exclusions found in the Business Auto Policy and discuss Physical Damage coverage. The objectives are to ensure that you can apply the liability exclusions, as well as the physical damage exclusions, in specific situations. In addition, you will be able to determine how specific policy conditions apply in differing circumstances. Let's continue our review of the liability exclusions by looking at the sixth exclusion found in the BAP.

The **Care, Custody, or Control exclusion** eliminates liability coverage for damage to property that belongs to the insured, is being transported by the insured, or that the insured has in their custody or care. For example, think of a brake repair shop accidentally damaging a customer's car during a test drive. The brake shop's BAP will not pay for the damage. A different kind of insurance is needed in this example. The insurance is called Garagekeeper's and it is a type of bailee insurance. Likewise, a business that has the property of others in or on its vehicles would have no liability coverage under the BAP for damage to that property or cargo. In this scenario, an inland marine insurance type called transportation insurance would be needed.

Handling of Property is the next exclusion. The BAP policy is designed to provide liability coverage for bodily injury or property damage arising from the operation of covered autos. That liability includes loading and unloading of the covered auto. The Handling of Property exclusion clarifies that there is no coverage before the loading starts or after the unloading is completed.

This is an important distinction because the facts of an accident can determine whether the bodily injury or property damage from the accident should be paid by the Commercial General Liability policy or the BAP. The exclusion states that it applies, "before it is moved from the place where it is accepted by the insured for movement into or onto the covered auto" and "after it is moved from the covered "auto" to the place where it is finally delivered by the insured." So, before it is moved during the loading process, accidents would be covered under the CGL. Likewise, after it is set down during unloading, it is also covered under the CGL. Accidents between and during the trip on the covered auto, would be a claim under the BAP.

Since the BAP is designed to provide liability coverage for loading and unloading of vehicles, the **Movement of Property by a Mechanical Device exclusion** removes coverage if that loading or unloading is performed using a mechanical device such as a

forklift. It does provide coverage if the device used was a hand truck, which may also be referred to as a dolly, or a mechanical device that is attached to the vehicle. The use of a forklift would be covered under the CGL.

The **Operations exclusion** is designed to eliminate liability coverage for the operation of two types of equipment. The first is mobile equipment, as stipulated in the definitions section of the policy. The second is machinery or equipment that is on, attached to or part of a land vehicle that would qualify under the definition of mobile equipment if it were not subject to a compulsory or financial responsibility law or other motor vehicle insurance law where it is licensed or principally garaged. What this means is that the operation of certain equipment, such as cherry pickers used to raise or lower workers, air compressors, pumps, generators, and similar types of machinery or equipment are excluded on the BAP.

The operation of the types of equipment mounted on a truck, such as a bucket, are liability exposures that are covered under the Commercial General Liability policy. So, when a truck is stopped and the workers are working in the bucket, the exposure is a CGL exposure. When the truck is going down the road, an accident involving the bucket would be covered by the BAP because it is an extension of the truck while it is in motion.

Mobile equipment, as defined in the policy, includes machinery and equipment such as bulldozers, farm machinery, or forklifts, which are all covered under the CGL. So the BAP typically won't respond. However, there are some types of equipment that occasionally travel on public roads even though they weren't designed for that purpose. In some states, this type of machinery and equipment is required to be insured for liability on an auto policy. As you may recall, these are the types of vehicles that would be covered using Symbol 19. The operation of these types of vehicles would have liability protection under the BAP.

The BAP policy was not designed to provide coverage for liability arising out of the **completed operations** of the insured, even when those completed operations are related to auto repair and servicing. Keep in mind that the BAP is solely providing coverage for covered autos. The CGL policy and the Garage policies provide coverage for completed operations.

The **Pollution exclusion** is lengthy, so we'll look at it in very general terms. In brief, the BAP eliminates any liability relating to a pollution event involving a covered auto. However, there are two exceptions. The first exception is if the pollutants come from the operational systems of the covered auto itself – for example the fuel, oil, or hydraulic fluid – as a result

of an accident, then coverage for bodily injury, property damage, and covered pollution costs apply. The second exception is if an accident occurs away from the insured's premises – the pollutants are not in or on a covered auto – AND the discharge of pollutants was caused by the accident involving the covered auto, then covered pollution costs apply.

For example, let's say that an insured accidentally backs their covered auto into a storage tank located on their business property. When the chemicals in the storage tank leak into a neighboring creek, there is no coverage under the BAP. On the other hand, imagine that the insured is driving their covered auto and accidentally strikes an oil tanker truck on the highway. The accident causes the tank to rupture and dump many barrels of oil onto a nearby property. In this case, the claim would be covered.

The last two liability exclusions are for **war** and **racing**. It is common in all policies for damage as a result of war or warlike actions to be excluded. The Racing exclusion applies to any organized racing or stunt activities, including any practice, or even preparation.

OK, now that you have learned about the basic liability coverages, as well as the exclusions, let's talk about limits. In the BAP, the limit which is shown in the declarations, is the most that would be paid for any one accident, regardless of the number of covered autos involved, insureds, or claims made. Also note that there is no duplication of payments for the same elements of the loss.

Physical Damage Coverage

Now let's turn our discussion to the Physical Damage coverage provided in the BAP. As opposed to liability coverage, physical damage provides protection from direct and accidental loss or damage to an insured's owned autos, and their equipment. With the selection of proper symbols, sometimes a hired or borrowed auto may also be covered for physical damage. The three types of physical damage coverage are collision, comprehensive, and specified causes of loss. The coverage is triggered on the Declarations page by the use of the correct symbol for the coverage desired. For example, an insured may decide to insure an old vehicle under a less expensive type of coverage, and the new vehicle with broader protection. As you can see, which symbols are assigned to which vehicles becomes very important.

Let's begin by discussing the three primary coverages. **Comprehensive coverage**, the first coverage option, means any type of damage to the vehicle, EXCEPT for the covered auto's collision with another object or the vehicle's overturn. Consider the variety of ways a vehicle can be damaged by other than collision. For example, think of hail damage, theft,

vandalism, flood, or fire. Obviously, there are many perils other than collision, which is why this coverage is so important.

There are also perils that can damage the auto that technically would be a collision if not for the policy clarifying that these would be considered damages covered as a comprehensive loss. These perils are glass breakage, hitting a bird or animal, and falling objects or missiles. When you think of missiles, think of a flying rock thrown against the auto. The rationale for these exceptions is that insureds often carry lower deductible amounts for comprehensive coverage than they do collision claims, and these are common types of losses. So these types of losses are covered if the insured purchases comprehensive coverage.

Another physical damage coverage option is **specified causes of loss**. The policy lists the specified causes of loss perils. They are fire, lightning, explosion, theft, windstorm, hail, earthquake, flood, mischief or vandalism. This category also includes the sinking, burning, collision, or derailment of any conveyance that is transporting a covered auto. As you know, a conveyance could include a barge, a ferry, or any other form of transport between one place and another. Also, you may have surmised that given the limitations of specified causes of loss coverage, it is typically a lot less expensive than comprehensive coverage. You may have noticed that a common type of loss not covered by specified causes of loss is glass breakage.

The third physical damage option is **Collision**. This means that the policy will pay in the event of a covered auto's collision with another object or if the vehicle overturns. There are some areas in which the policy may not be entirely clear. As we mentioned previously, if your customer has comprehensive coverage, coverage for hitting a deer would be found here. If your client only has collision and specified causes of loss, hitting a deer is not under specified causes of loss, but may be covered under collision.

Other Coverages

Another coverage that is available under the BAP is for towing. **Towing coverage** is only available for private passenger type vehicles and includes the cost of labor if it is performed at the place of disablement. If your vehicle is damaged and your vehicle repair shop has a wrecker, any labor performed at the site will be covered.

The BAP provides two Coverage Extensions for Physical Damage. The first of these extensions is **Transportation Expenses**. This extension pays from twenty dollars per day up to a maximum of six hundred dollars total for the insured to secure temporary

transportation because of the total theft of a private passenger auto. For coverage to apply, the BAP must have coverage for Comprehensive or Specified Causes of Loss. Coverage does not apply to vehicles that only carry Collision coverage. There is a forty-eight-hour waiting period before coverage begins. The waiting period is included for the practical reason that many stolen vehicles are recovered within hours of the theft.

The second Coverage Extension is **Loss of Use Expenses**. This extension applies to Hired Autos only. If the Declarations page shows Symbol 8 next to a Physical Damage coverage applicable to the loss, the policy pays from twenty dollars per day to a maximum of six hundred dollars for the legal responsibility of the insured to pay for loss of use damages resulting from physical damage to a rented auto, or an auto hired without a driver. The obligation to pay loss of use damages must be in a written agreement.

Physical Damage Exclusions

The Physical Damage section of the BAP contains several exclusions: nuclear hazards, war, military action; professional or organized racing, demolition contests, and stunt activities, including preparation or practice for these. It also excludes wear and tear, freezing, mechanical or electrical breakdown, blowouts, punctures, or other road damage to tires. Another exclusion is loss to equipment, such as tapes, records, CDs, or other audio-visual or data devices and speed measuring or jamming equipment. Finally, loss is also excluded for equipment that reproduces, receives, or transmits audio, visual, or data signals, as well as the equipment's accessories. There are exceptions built into the exclusion that provides coverage if the equipment is permanently installed.

The last exclusion is for diminution in value. Diminished value is the loss in value of a vehicle, even after repairs are completed, from an accident. In short, a wrecked and repaired vehicle is simply not as valuable as the same vehicle that had never been in an accident. For example, a private passenger vehicle is damaged in a collision and then repaired. Before the loss, the actual cash value of the auto was twenty thousand dollars. After the loss and the repair, because the vehicle has a record of being damaged, it has an actual cash value of sixteen thousand dollars. The BAP will not provide coverage for this loss in value.

Payment under Physical Damage Coverage

The BAP contract outlines how much will be paid under Physical Damage coverage. The policy will pay the lesser of the actual cash value of the damaged or stolen property at the time of the loss, or the cost to repair or replace damaged or stolen property with other property of like kind and quality. For example, if Jane's car is heavily damaged, the

insurance company is going to look at how much the car was worth before the loss compared to what it would cost to repair the car. They will pay Jane the lesser amount of the two.

An insurance company is not obligated to pay for betterment of the auto. For example, a company is not obligated to replace a vandalized convertible top with a new convertible top, unless there is no other option. When calculating the actual cash value, an insurance company considers how much a vehicle has depreciated. Depreciation is the amount of value the auto has lost due to its age, mileage, or wear and tear.

As you may have guessed, there is typically a deductible for each Physical Damage loss under the BAP. The deductible is the amount the insurance company reduces its payment for a loss, and it is shown in the Declarations page for each coverage. For example, say the actual cash value of a vehicle before a loss is \$5,000, and repairing the vehicle will cost \$6,000. The value of the vehicle as damaged is \$1,500. There are two options here. The insurance company can pay the insured the actual cash value of \$5,000, minus the deductible, and then sell the damaged auto for what they can get, or \$1,500. The other option is for the insured to keep the auto and receive a payment of \$3,500, less the deductible. That is the actual cash value minus what the damaged vehicle is worth. If the insured selects this option, they will keep the auto, take the payment, and repair the vehicle if they choose to do so.

As you are aware, the Conditions of an insurance contract outline the rules of how the contract works. Each condition describes the obligations of the parties, should there be a loss. The BAP Conditions include five specific rules regarding appraisal of the loss, and what the parties do if there is a disagreement. The first condition outlines how losses will be appraised. The next condition outlines the duties the insured has in the event of a loss, including reporting of the loss, cooperating with the insurance company's investigation of the loss, and authorizing the insurance company to obtain important information, and submitting to examination under oath. The third condition focuses on conditions under which the insured can start legal proceedings against the company, and the fourth outlines the payment of physical damage losses. The fifth condition states that the insured may not transfer their rights of recovery against others after the loss.

There are additional conditions such as bankruptcy, concealment, misrepresentation, or fraud that are discussed. There are also rules that apply if other insurance covers the loss. There are four situations in which the BAP coverage is the primary coverage. Primary coverage means it pays first. If an auto is owned by the insured, the BAP coverage is

primary. The BAP coverage is also primary in the event that a trailer is attached to a covered auto. Because any hired auto can be considered owned, physical damage to a hired car can be paid with the BAP as primary. Finally, any liability the insured assumed under an insured contract is primary. In other situations, the BAP provides excess coverage, meaning that it pays AFTER the owner of the auto's insurance has paid.

Other important conditions of the BAP are the Policy Period and the Coverage Territory. These conditions describe when and where a contract applies. The Policy Period is described in the Declarations with a beginning date and an expiration date. The Coverage Territory of the policy is the USA, its territories and possessions, as well as Puerto Rico and Canada. There are also situations where coverage could apply in other places for a limited time, and with conditions. OK, we've covered a lot today, so complete the activities to solidify your understanding of this material.