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Jeffrey W. Stempel

University of Nevada, Las Vegas – William S. Boyd School of Law

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REDISCOVERING THE SAWYER SOLUTION: BUNDLING RISK FOR PROTECTION AND PROFIT

Jeffrey W. Stempel*

*Doris S. & Theodore B. Lee Professor of Law, William S. Boyd School of Law, University of Nevada Las Vegas. Thanks to Matthew Beckstead, Craig Berrington, William S. Boyd, James Davey, Elizabeth Ellison, Chris French, Dan Hamilton, Peter Kochenburger, Mary Langsner, Doris Lee, Ted Lee, David McClure, Ann McGinley, Peter Molk, Jeanne Price, Nancy Rapaport, Jim Rogers, Dan Schwarcz, Steven Weisbart, Harold Weston, John White and especially to Jay Feinman, Adam Scales, Rick Swedloff, and the *Rutgers Journal of Law & Public Policy* for their efforts bringing about this conference and collection of papers. © 2013 Jeffrey W. Stempel.

INTRODUCTION

One of the fascinating, but disheartening aspects of history is the manner in which some persons or events are continually trumpeted, even if overrated, while others are too quickly forgotten. Everyone knows about Bunker Hill, but the Battle of Saratoga was more important in turning the American Revolution in favor of the colonies that would become the United States. Generals George Smith Patton, Jr. and Douglas MacArthur continue to survive in everyone's collective memory, while George C. Marshall, and increasingly his Marshall Plan that essentially saved post-War Europe, are often overlooked. Babe Ruth remains a household name, while Lou Gehrig is most associated with a terrible disease, even though Gehrig was a comparably valuable baseball player.

Recently, the fall of false idol Lance Armstrong revealed how quickly a true trail-blazing cyclist, who preceded Armstrong, has faded prematurely from public memory. According to the typical narrative, the now-disgraced former seven-time Tour de France champion, Armstrong, was the first to put cycling on the map in the United States. The problem with this narrative is that it unfairly overlooks Greg LeMond, who won the Tour de France three times, twice after a near-fatal hunting accident that led to a two-year hiatus before his return. This was highlighted by a dramatic closing-day come-from-behind win by the closest margin in the history of the event.¹

¹ LeMond may have lacked Armstrong's public relations flare and sustained streak of (apparently substance-aided) wins, but LeMond's victories earned him at least one *Sports Illustrated* cover (and its designation as "Sportsman of the Year"), and lots of front page news coverage. See, e.g., Franz Lidz, *Vive Lemond!*, *SPORTS ILLUSTRATED*, Jul. 31, 1989, <http://sportsillustrated.cnn.com/vault/article/magazine/MAG1068628/index.htm> (emphasizing LeMond making up a fifty second deficit to lead during last day's time trial, an almost unheard of come-from-behind); see generally SAMUEL ABT, *LEMOND: THE INCREDIBLE COMEBACK OF AN AMERICAN HERO* (1990) (LeMond lauded for returning to top cycling form after near-fatal hunting accident); PETER NYE, *HEARTS OF LIONS: THE HISTORY OF AMERICAN BICYCLE RACING* (1988) (LeMond viewed as key figure in modern American cycling); SAMUEL ABT, *UP THE ROAD: CYCLING'S MODERN ERA FROM LEMOND TO ARMSTRONG* (2007). In addition, LeMond has been an outspoken critic of the sort of doping to which Armstrong has now admitted after a decade of false denials. See David Epstein, *Kathy LeMond: Armstrong embarrassed, not truly sorry*, *SPORTS ILLUSTRATED* (Jan.

Insurance executive and attorney, Elmer Sawyer, who was a prime architect of the Comprehensive General Liability Policy,² was arguably a “Greg LeMond” of insurance (or perhaps a “Lance Armstrong” without the performance enhancing drugs), and seems to have suffered a similar fate. One has to get to high levels of an insurance company, or within that small group of academics active in the field, before anyone will recognize the name Sawyer. Even high-end coverage attorneys will draw a blank, save for the counsel to an elite policyholder who invokes his writings in favor of broad coverage,³ and his counterpart, who is at least forced to glance at Sawyer’s writings, while defending against such arguments.⁴

18, 2013), <http://sportsillustrated.cnn.com/more/news/20130118/lance-armstrong-admission-kathy-lemond-reaction/> (“In 2001, LeMond openly criticized Armstrong for his affiliation with Dr. Michele Ferrari, who is now banned for life from the sport. Armstrong subsequently began a campaign of disparagement against LeMond that included souring LeMond’s business relationship with the Trek bike company. Armstrong’s influence led Trek to drop its long time sponsorship of LeMond.”).

² See ELMER W. SAWYER, COMPREHENSIVE LIABILITY INSURANCE (1943). Woodhull Hay, the editor of a series of insurance source books published by the Underwriter Printing and Publishing Company during the 1940s, stated that, “Probably no one is better qualified to treat authoritatively of this complicated and fluid form [of general liability and the question of the scope of coverage] than E.W. Sawyer.” Woodhull Hay, *Editor’s Foreword* to ELMER W. SAWYER, COMPREHENSIVE LIABILITY INSURANCE (1943).

³ See, e.g., EUGENE R. ANDERSON ET AL., INSURANCE COVERAGE LITIGATION §1.01, at 1-6 n.11 (2d ed. Supp. 2004) (Sawyer initially cited and then cited frequently throughout chapter one regarding the origin of the CGL form); see also JEFFREY W. STEMPEL, STEMPEL ON INSURANCE CONTRACTS §14.01 (3d ed. Supp. 2013) (citing Sawyer frequently when describing origin and background of the CGL policy). But see, PETER J. KALIS ET AL., POLICYHOLDER’S GUIDE TO THE LAW OF INSURANCE COVERAGE (Supp. 2006) (example of a leading treatise that expressly examines insurance coverage from the policyholder’s perspective, without citing Sawyer).

⁴ However, a leading insurance coverage treatise, authored by insurer counsel, does not list Sawyer’s book or any of his writings in its table of authorities and appears not to cite Sawyer in its text. See BARRY R. OSTRAGER & THOMAS R. NEWMAN, HANDBOOK ON INSURANCE COVERAGE DISPUTES 1853-65 (13th ed. 2006); see also ALLAN D. WINDT, INSURANCE CLAIMS & DISPUTES: REPRESENTATION OF INSURANCE COMPANIES AND INSURED (Chris Kloeris et al. eds., 3d ed. 1995) (treatise authored by authority representing insurers in most instances does not cite Sawyer).

In this paper, I am not focusing on Sawyer as some sort of man-on-a-white-horse to which reverence is owed, nor do I suggest that he would have specifically or completely endorsed my proposals for a broader approach to the scope of coverage provided by insurance products. But Sawyer is an important figure in insurance history — one that deserves remembering, as does his approach to providing insurance in a manner that can benefit insurers and their constituencies. Sawyer was in favor of bundling, rather than disaggregating risks.⁵ My thesis is that this approach is correct, not only for general liability coverage, but also for insurance coverage in general. To paraphrase George Santayana, those who forget the past are condemned to repeat it⁶ — or at least to make mistakes that could have been avoided or minimized had there been a better sense of history.

The organizing theme of this *Fragmented Risk* conference is that insurance embodies a “tension between bundling risk and fragmenting risk.”⁷ In my view, the tension is one that can

⁵ See SAWYER, *supra* note 2, at 11 (“Liability insurance is now in the process of transition from the multiple separate covers to one comprehensive cover.”). Sawyer was something of a visionary, generally with eclectic sociopolitical views. Like other big business executives of the era, he disliked the New Deal and what he regarded as excessive government interference with free enterprise or undue forcing of economic outcomes. However, he was not an anti-regulation zealot, and he appreciated the important socioeconomic role of insurance. See Elmer W. Sawyer, *The Impact of the War on Existing Insurance Coverages (Other Than Life)*, A.B.A. SEC. INS. NEGL. & COMP. L. PROC. 26, 32 (1942). Sawyer also noted the impact of insurance limitations on business, *Id.* at 27–29, and predicted the emergence of the U.S. as “the dominant power” in the world after the War, despite the relatively recent Pearl Harbor attack and Axis success in conquest. *Id.* at 26, 29, 30. Additionally, Sawyer saw a post-War opportunity for U.S. insurers that could be seized by faster-acting U.K. insurers, *Id.* at 30–31, and he viewed the New Deal, and fascist movements, as anti-middle class and anti-free enterprise. *Id.* at 32. While he noted the important social impact of insurance, he also argued that insurance should ordinarily be provided by the private sector rather than by the government. *Id.* at 32–33. Sawyer stated, “[F]ree enterprise must be policed to prevent abuse.” *Id.* at 33.

⁶ See GEORGE SANTAYANA, *THE LIFE OF REASON* 82 (Prometheus Books 1998) (“Those who cannot remember the past are condemned to repeat it.”).

⁷ Program Announcement for a Conference on Fragmented Risk, Rutgers Ctr. For Risk and Responsibility, Rutgers Sch. of Law – Camden, (March 1, 2013), available at <http://camlaw.rutgers.edu/upcoming-risk-events> (last visited Nov. 17, 2013).

usually be successfully resolved in favor of bundling, which will normally provide insurance in a form more useful to policyholders, victims, society, and even insurers themselves. The organizers of this conference well-expressed this view:

Policyholders benefit from bundling risk because coverage is easier to purchase and more predictable, because there are fewer gaps in coverage and those gaps that remain are more easily understood. Insurers benefit because they insure a large number of policyholders with similar risk profiles so they benefit from the law of large numbers.⁸

Despite these undeniable benefits, the insurance industry appears to be moving away from risk consolidation to more narrow coverage of specified perils.⁹ Unlike Sawyer, the current

⁸ Kirk Hartley, *Great Questions About Insurance – Call for Papers for Rutgers Conference on Fragmented Risks Created by Current Forms of Insurance Sales*, GLOBALTORT (Oct. 26, 2012), <http://www.globaltort.com/2012/10/great-questions-about-insurance-call-for-papers-for-rutgers-conference-on-fragmented-risks-created-by-current-forms-of-insurance-sales/> (quoting original language used for conference announcement).

⁹ See Donald T. Hornstein, *The Balkanization of CAT Property Insurance: Financing and Fragmentation in Storm Risks*, 11 RUTGERS J. L. & PUB. POL'Y 1 (2013) (noting substantial fragmentation of property coverage, particularly in separation of windstorm and water damage coverage, and the rise of anti-concurrent causation clauses limiting coverage that was formerly available or at least arguable); see also Amy O'Connor, *Will Wind/Hail Cosmetic Damage Exclusion Endorsements Become the Norm?*, INS. J. (Mar. 7, 2013), <http://www.insurancejournal.com/news/national/2013/03/07/283640.htm> (noting movement toward stripping away coverage where damage to covered property can be deemed merely cosmetic); see also Christopher C. French, *The Aftermath of Catastrophes: Valuing Business Interruption Insurance Losses* (Vill. L. & Legal Theory Working Papers Series, Paper No. 3020, 2013) (noting a type of de facto reduction in coverage in that property loss and business interruption claims can be reduced by insurers assigning lower valuation to the loss and disputing claims); see also Michael Childress & Daniel Loucks, *The Hidden Conflict: The Secret Insurers Don't Tell Insureds* (Mar. 1, 2013) (manuscript), available at <http://www.riskworldwide.com/2013/03/the-hidden-conflict-the-secret-insurers-don-t-tell-insureds/> (insurers have economic incentive to unfairly deny or chip away at policyholder claims); see also Harold Weston, *A la Carte Coverage. Unbundling Causes of Losses and Coverage Grants to Allow Consumer-Insured Selection*, 11 RUTGERS J.L. & Pub. Pol'y __ (forthcoming Dec. 2013) (examining the prospect of increased policyholder ability to determine coverage contours and finding that, although promising in theory, it is likely to fall short in practice due to problems of consumer information and cognition, as well as unpredictability of risk); cf. Christopher C. French, *Profits Over Purpose: The Conflict in Insurance Law*

insurance industry seems to regard bundled insurance products that provide comprehensive coverage as a luxury the industry can no longer afford — or at least as a failure to grasp opportunities for enhanced profit and wealth maximization. Even those outside the industry, who are critical of the narrowed or inconsistent coverage, appear significantly more attracted to disclosure and policy transparency as a solution, rather than mandated minimally comprehensive coverage.¹⁰

Even when policies are generally broad in scope (or purport to be), the insurance policy may provide “Swiss cheese” coverage through a relatively broad insuring agreement, followed by a lengthy list of exclusions or policy provisions that operate as exclusions, to limit coverage based on the language of the policies’ definitions, conditions, or endorsements.¹¹ Insurers

Today (July 2013) (manuscript at 2-11) (describing contraction of coverage provided by general liability insurance during late twentieth century). In oral comments regarding my presentation, insurance economist Steven Weisbart, can be interpreted as at least an implicit endorsement of fragmentation, such that Dr. Weisbart argues that the broad approach favored by me (and, to a lesser extent, by Professor Weston) might risk the financial strength of an insurance industry that is not doing as well as I posit. Dr. Steven Weisbart, Senior Vice President and Chief Economist, Ins. Info. Inst., Fragmented Risk Symposium, Remarks to the Rutgers Ctr. for Risk and Responsibility (March 1, 2013).

¹⁰ See, e.g., Daniel Schwarcz, *Reevaluating Standardized Insurance Policies*, 78 U. CHI. L. REV. 1263, 1337-48 (2011) (making recommendations upon empirical analysis demonstrating wide variance in homeowners’ policies tending to create limitations on coverage, and emphasizing disclosure, transparency, and consumer choice before turning to “default” minimum coverage). See *infra* text accompanying notes (“TAN”) 265–269 (discussing disclosure as remedy for ineffective insurance).

¹¹ It is unclear who should receive credit for this popular means of describing insurance policies that purportedly provide broad cover, but are ridden with exclusions or limitations. See, e.g., The Byrd Law Firm, *Texas Homeowners Pay For “Swiss Cheese” Insurance*, (Jan. 16, 2013), <http://www.txbyrd.com/texas-homeowners-pay-for-swiss-cheese-insurance/>; Shipman & Goodwin LLP, *Environmental Insurance: Closing Coverage Gaps-Turning Swiss Cheese into Cheddar*, (Mar. 20, 2013), <http://www.shipman-goodwin.com/environmental-insurance-closing-coverage-gaps-turning-swiss-cheese-into-cheddar>; Bruce Cappon, *Will That Be Swiss Cheese Or Travel Insurance?*, CANADIAN MONEYSAVER, (Jan. 2012), available at http://www.firststrateinsurance.com/global/pdf/Will%20That%20Be%20Swiss%20Cheese%20Or%20Travel%20Insurance_Cappon.pdf (“Recognize a quality travel health policy from the Swiss cheese variety, the one riddled with holes

may further widen the “holes” in this Swiss cheese coverage through aggressive interpretations of coverage-limiting language.¹²

and exclusions.”); James Strickland, *Do You Have Swiss Cheese Liability Insurance?*, 61 CHILD CARE INFO. EXCH., May 1988, at 3. In any event, this Conference and Symposium have probably put the term “Swiss cheese” permanently into the academic literature. See Sam Friedman, *Fragmented Coverage Widens Knowledge Gap Among Consumers*, CLAIMS MGMT. (May 7, 2013), <http://claims-management.theclm.org/home/article/Fragmented-Coverage-Widens-Insurance-Knowledge-Gap> (noting that at the conference, “[o]ne plaintiff’s attorney in attendance complained that homeowners’ policies have so many exclusions that the industry has turned standard coverage into ‘Swiss cheese.’”). My recollection is that more than one Conference attendee had this view, which was not confined to plaintiffs’ counsel.

¹² See JAY M. FEINMAN, *DELAY, DENY, DEFEND: WHY INSURANCE COMPANIES DON’T PAY CLAIMS AND WHAT YOU CAN DO ABOUT IT* 62–63 (2010) (providing examples of aggressive insurer tactics in coverage disputes); French, *Profits Over Purpose*, *supra* note 9, at 30–33, 50–52. Although insurance bad faith law is supposed to limit such opportunistic behavior, the state-based nature of insurance law and many coverage decisions issued each year militate against this. Even if an insurer’s construction of a policy term or its conduct in handling a claim is suspect and at odds with prevailing practice, the insurer can usually point to at least a few judicial decisions — and probably some state supreme courts as well — that have occasionally accepted the insurer’s non-mainstream arguments, or at least deemed them a colorable construction of the policy language or type of policy at issue. See, e.g., *Village of Morrisville Water & Light Dept. v. United States Fid. & Guar. Co.*, 775 F. Supp. 718, 734–35 (D. Vt. 1991) (court notes that insurer makes this argument, which insurer contended precludes summary judgment for policyholder in bad faith claim based on failure to CGL insurer to provide coverage for government-ordered remediation pursuant to Superfund statute, an issue on which courts have diverged; Court, although not expressly endorsing argument, finds coverage for policyholder as a matter of law but denies summary judgment to policyholder regarding alleged insurer bad faith). See also *Ray, Inc. v. Nationwide Mut. Fire Ins. Co.*, 2013 U.S. Dist. LEXIS 31300 at *16–20 (D. Ala. Mar. 7, 2013) (insurer’s calculation of amount due policyholder “according to its normal procedures after an inspection by its adjuster and an engineer” for home damaged by storm precludes policyholder from prevailing in bad faith action alleging unreasonably low valuation; to win bad faith case, policyholder must show active misconduct by insurer in claims process).

In addition, since *State Farm Mut. Auto. Ins. Co. v. Campbell*, insurers have very little incentive (other than reputational concern), not to take chances with claims involving policies with low limits. 538 U.S. 408 (2003). Under *Campbell*, the practical maximum punitive award can be no higher than nine times the amount of compensatory damage suffered by the claimant alleging bad faith, at least when the amount of compensatory damages is substantial. *Id.* at 425; see generally JEFFREY W. STEMPEL, *LITIGATION ROAD: THE STORY OF*

In the not so recent past, however, the trend was in favor of bundling rather than fragmentation. Leading that trend on general liability coverage was Sawyer, a lawyer and insurance executive, generally viewed as the father of the comprehensive general liability (CGL) policy. The CGL has since been renamed the “commercial” general liability policy as an example of the industry’s modern retreat from broad coverage. Sawyer viewed the CGL’s broad grant of coverage as a means of aiding both the industry’s fight against adverse selection and its quest for increased premiums and profits, as well as a means of simplifying insurance sales practices and providing greater protection for commercial policyholders:

The objective of comprehensive liability insurance covering liability hazards other than those insurable under automobile liability policies is to afford, on as broad a basis as is feasible, protection against liability for any hazard not excluded The coverage can no longer be limited to the type of business in which the insured is engaged at the time the policy is written, but must follow his activities even though the nature of his business operations change completely. Consequently the coverage must apply automatically to all operations not specifically excluded.¹³

History has proven him right. Notwithstanding losses related to mass torts — such as asbestos, pollution, and drug product liability — the insurance industry has profited from the CGL format that has, despite its operational shortcomings, largely succeeded in providing both more extensive risk protection to policyholders and more expansive compensation to their victims.¹⁴ Perhaps because of the seemingly endless

CAMPBELL V. STATE FARM (2008) (prevailing in obtaining a \$145 million punitive damages plaintiff’s verdict, later set aside by the U.S. Supreme Court as noted above, in part because evidence suggested that insurance company had little incentive to honor policies issued to individual policyholders, absent possibility of very large punitive damages awards; Insurer’s revenue and wealth was so substantial that even multi-million dollar awards arguably had little deterrent effect).

¹³ See SAWYER, *supra* note 2, at 26–27.

¹⁴ See *infra* TAN 58–87; MARK R. GREENE, RISK AND INSURANCE 147 (4th ed. 1977) (stating standard form general liability and property insurance have been profitable products for insurers); Eliot Martin Blake, Comment, *Rumors of*

parade of asbestos claims still in the litigation pipeline, liability insurers have lost some of Sawyer's faith, while other areas of insurance appear equally or more fragmented.¹⁵

But the comprehensive approach has succeeded and can continue to succeed. In similar fashion to the CGL form, automobile insurance has largely been a success story¹⁶ — to the

Crisis: Considering the Insurance Crisis and Tort Reform in an Information Vacuum, 37 EMORY L.J. 401, 422–23 (1988) (stating insurers generally make sufficient amounts of money through investment to profit even when faced with significant underwriting losses); *but see* Weisbart, *supra* note 9 (arguing that safe and adequate investment income is not more difficult for insurers to achieve in the current low interest rate environment).

¹⁵ See *infra* TAN 127–188 (describing contraction of former breadth of CGL coverage and fragmentation of other insurance lines).

¹⁶ Although automobile liability insurers often have a combined ratio (total claims costs and administrative expenses expressed as a fraction over premiums received) or even a loss ratio (total claims costs expressed as a fraction over premiums received) exceeding 1.0, or 100 (authors and organizations differ in their numerical preference), most auto insurers are quite profitable due to investment income earned on premium dollars for months, years, or even decades before a claim is incurred or paid. See MARK S. DORFMAN & DAVID A. CATHER, INTRODUCTION TO RISK MANAGEMENT & INSURANCE 58 (10th ed. 2013); HAROLD D. SKIPPER & W. JEAN KWON, RISK MANAGEMENT AND INSURANCE: PERSPECTIVES IN A GLOBAL ECONOMY 500–05 (2007); SCOTT E. HARRINGTON & GREGORY R. NIEHAUS, RISK MANAGEMENT AND INSURANCE Ch. 13 (Michele Janicek ed., 2d ed. 2004); EMMETT J. VAUGHAN & THERESE M. VAUGHAN, FUNDAMENTALS OF RISK AND INSURANCE Chs. 2– 3, 5, 7–8 (8th ed. 1999) (describing, generally, the business model of insurance in which carriers can profit overall, even if spending more on claims than amount of premiums received); see also JEFFREY W. STEMPEL ET AL., PRINCIPLES OF INSURANCE LAW 16–17 (4th ed. 2011). Furthermore, a number of automobile insurers (e.g., GEICO of televised lizard fame) have a combined ratio of less than 100, suggesting they are quite profitable overall. See *Top 100 Groups Ranked by Net Premiums Written*, PROP. CASUALTY 360: NAT'L UNDERWRITER, Jul. 2013, at 34, 34–35 (stating GEICO parent Berkshire Hathaway Group had a combined ratio of 91.87 in 2012; major insurance groups often had combined ratios of less than 100 in 2012 and 2011, which means that they were profitable even without consideration of investment income, which historically is the chief driver of insurer profits); see also A.M. BEST CO., INSURANCE FACTS AND STATS: AN INTRODUCTION TO THE INSURANCE INDUSTRY 14 (Laura McArdle ed., Supp. 2012 ed.) (stating that the combined ratio has generally been at or slightly below 100 for auto insurers overall during the past decade); *Top 100 Groups*, *supra*, at 34–35 (describing that many of the largest insurers with combined ratios of less than 100 reflect profitability even without consideration of investment income during time between receipt of premium and payment of claim).

extent one can have a success story within the confines of a system that provides an inadequate social services safety net, and instead relies heavily on tort litigation for compensation and regulation.¹⁷

Even regarding liability insurance, and perhaps especially for property insurance (such as homeowners' policies), the "melting pot" of insurances has hardened or reversed itself, although commercial and marine risks appear to continue to be written on an all-risk basis.¹⁸ The "wind vs. water" conundrum associated with Hurricane Katrina claims is a dramatic example of the failure of fragmented coverage, but other examples abound.¹⁹ The continuing failure to integrate flood, earthquake,

¹⁷ Because of the low liability minimum policy limits required in most states and the degree of uninsured drivers, notwithstanding state financial responsibility laws, one can certainly question whether auto insurance has worked well as a matter of social policy. See ANDREW TOBIAS, *THE INVISIBLE BANKERS: EVERYTHING THE INSURANCE INDUSTRY NEVER WANTED YOU TO KNOW* 197–204, 276–77 (1982) (criticizing prevailing auto insurance regime and recommending a "pay at the pump" system, similar to the system of New Zealand, where auto coverage is funded by a gasoline tax); Marc Lifsher, *State Starts Crackdown on Uninsured Drivers*, L.A. TIMES, Dec. 6, 2006, <http://articles.latimes.com/2006/dec/06/business/fi-suspend6>; Study: *Uninsured Driver Problem Costs Oklahoma \$8.8M a Year*, INS. J. (Jan. 9, 2013), <http://www.insurancejournal.com/news/southcentral/2013/01/09/276807.htm>; *News Release: Recession Marked by Bump in Uninsured Motorists*, INS. RES. COUNCIL (Apr. 21, 2011), http://www.insurance-research.org/sites/default/files/downloads/IRCUM2011_042111.pdf ("Across the United States, chances are roughly one in seven that a driver is uninsured . . ."); Larry Copeland, *One in Seven Drivers Have No Insurance*, USATODAY, Sept. 11, 2011, <http://usatoday30.usatoday.com/news/nation/story/2011-09-11/uninsured-drivers/50363390/1>. But these arguable failures of auto insurance, which hardly indicate a complete failure of the system, have not prevented auto insurers from profiting with an approach that essentially parallels Sawyer's view of the CGL policy.

¹⁸ See Weston, *supra* note 9 (describing broadening of property and automobile insurance in similar fashion to the CGL movement during mid-twentieth century); French, *Profits Over Purpose*, *supra* note 9, at 27–29; see also ROBERT H. JERRY, II & DOUGLAS R. RICHMOND, *UNDERSTANDING INSURANCE LAW* § 13A[a], at 29–30, § 60A, at 391–92 (4th ed. 2007) (identifying marine, life, and liability insurance as essentially written on an all-risk bases); GEORGE E. REJDA, *PRINCIPLES OF RISK MANAGEMENT AND INSURANCE* 109 (9th ed. 2005).

¹⁹ See *infra* TAN 199–203; French, *Profits Over Purpose*, *supra* note 9, at 29 (describing Hurricane Andrew's responsibility for \$23 billion in losses in 1992, Hurricane Wilma's responsibility for \$23 billion in losses in 2005, and

and other property coverage, along with the segmentation of insurance products overall, underscores how little has been accomplished in spite of Katrina and other disasters. Only life insurers appear to have followed the Sawyer model — and it has been a successful model for them,²⁰ although life insurance is as much of a financial investment activity as one of risk-spreading, regarding the risk of premature death.²¹

In addition, some specialized policies linked to death (e.g., flight insurance, accident insurance, burial insurance) are narrowly drawn.²² However, these insurance products are notoriously bad deals for their purchasers²³ (and perhaps for

Hurricane Katrina's cause for \$43 billion in losses); *see also* Bradley G. Bodiford, *Florida's Unnatural Disaster: Who Will Pay for the Next Hurricane?*, 21 U. FLA. J.L. & PUB. POL'Y 147, 149, 156, 161–62 (2010).

²⁰ The typical life insurance policy provides death benefits without regard to the cause of death, subject to a small (as compared to other insurance products) number of exclusions involving dramatic risks such as death in combat. *See* DORFMAN & CATHER, *supra* note 16, at 168; REJDA, *supra* note 18, at 109; VAUGHN & VAUGHN, *supra* note 16, at 262.

²¹ *See* DORFMAN & CATHER, *supra* note 16, at 227.

²² Flight insurance, for example, provides life insurance coverage for the passenger/policyholder, but only for the time when the passenger is en route. Similarly, accidental death insurance only covers death caused by an accident and excludes death due to disease or natural causes. The somewhat misnamed burial insurance (more properly called industrial life insurance) is a small face-value general life insurance policy that normally covers death due to any cause, but provides such small benefit amounts that the policy proceeds are largely consumed by burial expenses, hence the name. *See* JERRY, II & RICHMOND, *supra* note 18, § 13A[2], at 35–36.

²³ These narrower versions of life products are inferior because they provide the policyholder with only limited protection, but do so at a cost that is relatively high for the amount of coverage received when compared to comparable regular life insurance. For example, a flight insurance policy provides coverage only if the life insured perishes on a particular flight. Even for long flights to Europe or Asia, this means coverage lasts only for hours and perhaps maximally a day or two. In return, the purchaser typically pays a premium per thousand dollars of coverage that would buy a much longer period of regular life insurance coverage, which would also insure against the risk of death by nearly any cause during that time period (save for extraordinary risks such as war), not merely the risk of crashing while on a particular flight. *See* ROBERT H. JERRY II & DOUGLAS R. RICHMOND, UNDERSTANDING INSURANCE LAW §32[c] (discussing flight insurance, which limits coverage only to death occurring as a result of

beneficiaries as well).²⁴ These products serve to again illustrate the superiority of bundling and broad-based policies — at least if the goal of effectively providing insurance is as important as wringing all possible profits from the enterprise.²⁵

A more comprehensive approach to writing risk coverage would serve the legitimate interests of insurers and society, while reducing opportunistic behavior by insurers.²⁶

crashes involving particular flights or over a short time period, as a form of “Vending Machine Insurance,” although the product may also be sold at kiosks in airports); Jeffrey W. Stempel, *Timeless and Ahead of Its Time: Lachs v. Fidelity & Casualty of New York*, 2 NEV. L.J. 319 (2002)(describing nature of flight insurance and leading case involving this product).

²⁴ For the reasons noted in note 23, the beneficiary of a flight, accident, or burial insurance policy would have been better off if the policyholder/CQV had used the same amount of premium dollars to purchase a standard life insurance policy. This is because the standard life insurance policy would have provided a larger policy limit, as well as created fewer opportunities for the insurer to question coverage (e.g., whether the death of an individual was the result of an “accident” or due to natural causes).

In addition, the narrow and specialized nature of these policies provides additional risk of post-death coverage disputes. *See, e.g., Lachs v. Fid. & Cas. Co. of N.Y.*, 118 N.E.2d 555 (N.Y. 1954) (dispute regarding application of language limiting coverage to flights on “scheduled” airlines results in denial of coverage successfully overcome by beneficiary, with court split and devoting substantial resources to resolving dispute); *see also* STEMPEL, ET AL., *supra* note 16, at 187–95 (excerpting *Lachs* as example of problems presented by vending machine-style marketing of policy at airport); Jeffrey W. Stempel, *Timeless and Ahead of Its Time: Lachs v. Fidelity & Casualty Co. of New York: Timeless and Ahead of Its Time*, 2 NEV. L.J. 319, 320–21 (2002) (finding *Lachs* correctly decided in favor of coverage, but noting strongly respected opinion to the contrary, and difficulty presented by marketing of flight insurance as well as language used to limit insurer risk).

²⁵ In the interests of time and space, this paper assumes that there is reasonable agreement that insurance, probably more than most enterprises is affected with a public interest, and that the overall impact on society of a more comprehensive, as opposed to a more fragmented model of insurance, is as legitimate a consideration as the profitability of insurers.

²⁶ When insurance products are more fragmented and complex, with more restrictions on coverage, insurers are presented with more borderline cases of coverage and hence, greater discretion to accept or reject coverage. This discretion can be influenced by the size of the claim as well as the importance of retaining the goodwill and business of the policyholder in question. This also provides the insurer with further opportunity to engage in opportunistic behavior, including the denial of claims or the making of inadequate settlement

Unfortunately, the insurance industry has been moving in the opposite direction and may never again duplicate the mid-twentieth century feat of Sawyer and liability insurers, unless the industry is prompted by government regulation aided by apt judicial resolution of coverage disputes. Regulation can be justified on economic, psychological, and moral grounds, despite objections of the industry and defenders of market-based product development. Furthermore, despite insurer resistance, a comprehensive approach can be an effective route to profitability and sound public policy.

Part I of this article describes the background and theory of the CGL policy. Part II describes the success of CGL and its comprehensive approach, successfully taking place in spite of the asbestos mass tort and other liability challenges of the late twentieth and early twenty-first centuries. Part III notes the success of other comprehensively written insurance products during the twentieth century. Part IV addresses the retreat from the comprehensive approach in general liability insurance and other property/casualty lines. Part V proposes a recommitment to the comprehensive coverage ideal and argues that a more comprehensive approach not only serves policyholder and public interest, but also serves insurer business interests as well. Part V addresses the role of regulators, courts, and the insurance industry's effect on a movement back toward comprehensive coverage.

I. SAWYER'S APPROACH TO RISK AND THE EMERGENCE OF THE CGL

The CGL policy²⁷ has its roots in the 1930s and was established during the 1940s.²⁸ The first standardized CGL

offers as a response strategy. When the policies are sufficiently fragmented and complex, even harsh coverage denials or claims practices can often be sufficiently defended so that an assessment of bad faith damages against the insurer is unlikely.

²⁷ The renaming of the CGL from "Comprehensive" to "Commercial" General Liability policy took place in the 1986 revisions to the CGL, as the insurance industry sought to avoid the broad coverage connotation of the word "comprehensive." As stated in Part 1 of this article, the advent of the CGL policy is more extensively discussed in STEMPER, *supra* note 3, § 14.01, and Jeffrey W.

form, crafted by the National Bureau of Casualty and Surety Underwriters and the Mutual Casualty Insurance Rating Bureau, was issued in 1941.²⁹ In 1943, a revised standard CGL form was issued and became widely used. The CGL policy was revised again in 1947, and significantly revised in 1955, 1966, 1973, and 1986.³⁰ The two rating bureaus that crafted the CGL policy eventually merged into the Insurance Services Office (“ISO”). ISO continues to draft subsequent revisions to the standard form CGL.³¹

Liability insurance is “a relatively new line” of insurance coverage that began in the late nineteenth century in England.³² During the first part of the twentieth century, various types of more sophisticated liability insurance products arose: Public Liability Insurance; Owners’, Landlords’, and Tenants’ Public Liability Insurance; Manufacturers’ Public Liability Insurance; Contractors’ Public Liability Insurance; Contractual Liability Insurance; Owners’ Protective Liability Insurance; Contractors’ Protective Liability Insurance; Premises and Operations Insurance; and other separate liability insurance coverages.³³ The CGL policy is derived in significant part from Public Liability Insurance and Premises and Operations Insurance, but with additional, more inclusive coverages, as implied by the name “comprehensive.” At roughly the same time, insurers also began to offer defense of liability claims as part of the insuring agreement.

Stempel, *Assessing the Coverage Carnage: Asbestos Liability and Insurance After Three Decades of Dispute*, 12 CONN. INS. L.J. 349, 355–58 (2006).

²⁸ See SAWYER, *supra* note 2, Ch. 3 (1943); *Insurance Issues and Superfund: Hearing Before the U.S. Senate Comm. on Env’t & Pub. Works*, 99th Cong. 149 (1985) (statement of Richard A. Schmalz, Am. Ins. Ass’n).

²⁹ See SAWYER, *supra* note 2, Ch. 2.

³⁰ See EUGENE ANDERSON ET AL., *supra* note 3, § 1.02 (noting less significant revisions of the CGL in 1988, 1990, and 1993).

³¹ See KENNETH S. ABRAHAM, *INSURANCE LAW AND REGULATION: CASES AND MATERIALS* 34 (4th ed. 2005).

³² See ALBERT H. MOWBRAY ET AL., *INSURANCE: ITS THEORY AND PRACTICE IN THE UNITED STATES* 233 (6th ed. 1969).

³³ See SAWYER, *supra* note 2.

Prior to the advent of the CGL policy, the aforementioned types of liability insurance listed above were each sold separately.³⁴ This presented difficulties for both insurers and policyholders. Insurers disliked the increased potential for adverse selection by policyholders, who might purchase only coverage more likely to be needed, while refusing to buy other coverages, thereby depriving insurers of potential premium dollars.³⁵ This also raised pricing problems and fairness issues because some customers subsidized the coverages of others. It was also thought that presenting this much choice to some policyholders would encourage unduly risky behavior as policyholders gambled on the types of coverages they would need. Rating the multiple coverages was also difficult because of the narrow focus of risk assumed and the smaller pools of premiums for collection and investment.³⁶

In response to the problems of splintered policies and coverages, the liability insurance industry developed the CGL policy. Instrumental in the process was Sawyer, an attorney for the National Bureau of Casualty and Surety Underwriters prior to its merger with the Mutual Insurance Rating Bureau to form the ISO. Explaining the rationale for the move toward consolidated liability coverage, Sawyer wrote:

Whereas, in the past we have offered multiple separate liability covers, each excluding hazards within other covers and each being optional with the insured, and have insured only against hazards within the covers chosen by the insured, we now insure against all of the hazards within the scope of the insuring clause which are not specifically mentioned as excluded. Stated differently, instead of insuring against only enumerated hazards we now insure against all hazards not excluded. . . .

³⁴ *Id.* at 13.

³⁵ *Id.* at 14.

³⁶ *Id.* at 12-18.

Liability insurance is now in the process of transition from the multiple separate covers to one comprehensive cover.³⁷

In addition to creating something closer to “one stop shopping” for businesses, risk managers, and brokers, the CGL policy was also designed to help insurers manage their liability exposure and to accept risk transfer profitably. Sale of the more expansive and bundled CGL policy required business policyholders, in many cases, to buy more insurance and pay more premiums than would otherwise have been the case.³⁸

³⁷ *Id.* at 11.

³⁸ *Id.* at 135 (“[CGL] insurance offers opportunities for the producer to increase his own income through the placing of additional insurance”); *Id.* at 145 (“[T]he producer should do his utmost to place comprehensive liability insurance with every risk that has a need for it. Few businesses are too small to need it or to make it unprofitable to the producer to sell it.”); Thomas M. Reiter, et al., *The Pollution Exclusion Under Ohio Law: Staying the Course*, 59 U. CIN. L. REV. 1165, 1223–24 (1991) (CGL policy was sold as comprehensive policy providing “peace of mind” for policyholders for which insurers in turn demanded and received larger premiums); John H. Eglof, *Liability Insurance, The Outside*, BEST’S FIRE & CAS. NEWS, May 1941, at 19–20, 56–57 (arguing that bundling of liability coverages into comprehensive policy would enable insurers to obtain greater premium volume by encouraging sale of broad coverage product rather than more selective insurance purchases by policyholders; citing example of initial liability insurance premium of \$10/year that could be “built up” to annual premium of \$700 for comprehensive policy; Eglof was Supervisor of the Agency Field Service of The Travelers Insurance Company.).

It appears that Sawyer and Eglof were not only aware of the potentially greater profits from CGL sales, but also genuinely saw the broad coverage product as better for policyholders, and even society. In a bit of hyperbolic boosterism that now seems part of a bygone era, Sawyer stated that “[i]f every producer would make a real effort to sell [CGL coverage] to every business on his books, he would be making a contribution toward the solution of war and postwar problems of far-reaching importance.” See SAWYER, *supra* note 2, at 145–46. Although Sawyer’s appeal seems more than a little overwrought, his sincerity appears genuine. He consistently argued for the mutual advantage (for insurer and policyholder) of the comprehensive approach and sought to have insurance move toward a supremely comprehensive all-risk model.

There seems to be little doubt that the ultimate goal is an “all risk” liability policy. Such a policy would cover all liability hazards of the insured. It would not be limited in any way except to tort liability [It] is still far in the future . . . [and requires] a long series of intermediate steps [but is] the general direction in which we are traveling.

See SAWYER, *supra* note 2, at 115–16.

These greater premium receipts could be used by insurers to earn more money on investment of premium dollars. In the 1940s, as today, insurers made much of their profit on the “float” of holding premium dollars as investments for many years before they were typically required to pay claims.³⁹

Without a doubt, the object of the insurance industry, in crafting the CGL, was to offer for sale an attractive product providing comprehensive insurance protection in order to both reduce adverse selection and to encourage greater premium payments by policyholders. An insurance company executive, writing at the time of the promulgation of the CGL policy, emphasized its breadth of coverage:

[With the CGL policy form, the] burden of determining what to insure and what not to insure is removed from the shoulders of the insured and

³⁹ Insurers make substantial profits because of the time value of the funds they hold due to premium payments. Insurers profit from this “float” and investment income for years prior to paying claims. Even where the amount of claim costs exceeds premium collections, insurers typically make money because of earnings on these collected premiums prior to payment of related claims costs. Warren Buffett, who has described his company, Berkshire-Hathaway, as primarily an insurance company, notes that the insurers owned by Berkshire-Hathaway earn most of their profits, not from underwriting, but from the float of premiums collected well before claims are paid under the policies for which those premiums were charged. See Letter from Warren Buffet, Chairman of the Board, to Shareholders of Berkshire Hathaway Inc., (Feb. 28, 2001), available at <http://www.berkshirehathaway.com/letters/2000pdf.pdf>. Buffet makes a similar observation, in varying degrees of detail, in nearly every one of his annual letters to shareholders issued during the past two decades. See also Richard E. Stewart & Barbara D. Stewart, *The Loss of Certainty Effect*, 4 RISK MGMT. & INS. REV. 29, 32 (2003) (insurers have explicitly recognized that “the earnings on funds reserved for claims [are] the most significant component of earnings for a property-liability insurance company.”). Additionally, “[i]nsurance managements are more than sufficiently intelligent to see that delaying the payment of claims increases the float period and denying claims decreases the cost.” *Id.* See generally SCOTT E. HARRINGTON & GREGORY R. NIEHAUS, RISK MANAGEMENT AND INSURANCE 123–25 (Michael W. Junior et al. eds., 1999) (insurers profit on investment income and delayed payment of claims; underwriting cycles can vary according to changes in investment return, and in reaction to previous pricing strategies as well as “capital shocks” from large losses); GREENE, *supra* note 14, at 147 (“In property and liability insurance, investment income has accounted for a very substantial portion of total profits and has served to offset frequent underwriting losses.”).

placed squarely on the producer and the carrier. How much better it is to say — “We cover *everything* except this and this and this” — instead of “We cover *only* this and this and this.”

No longer will an insured with Owners’, Landlords’ and Tenants’ coverage in one company and Elevator coverage in another company take them both to court to prove where the claimant fell down. . . .

Since a risk cannot choose the kind of accident that will give rise to the need for liability insurance, it is wise to be protected against all losses under one policy — *One policy — one premium and worry regarding liability insurance is off his mind.*⁴⁰

The CGL policy was structured with a broad insuring agreement, but then utilized exclusions as necessary to protect insurers from certain risks. The exclusions in the CGL policy are provisions that narrowed the scope of coverage. For example, intentionally caused injury was excluded, as was liability assumed by contract, automobile, aircraft, or watercraft liability, employee injuries, and damage to the policyholder’s own property or own products.

The insurer impulse to broaden coverage in the CGL policy (but to be correspondingly paid higher premiums for the greater coverage), continued during the first quarter-century of its use. The original CGL policy provided coverage where an injury giving rise to a liability claim was “caused by accident.” The term “accident” was not defined in the original CGL policy, the 1943 CGL form, the 1947 form, or the 1955 form. Courts are divided significantly on the question of whether an injury-producing event must be discrete and isolated in order to constitute an “accident.” An emerging, but not overwhelming, majority of courts concluded that an “accident” need not be confined in time and space and could be an injury-producing

⁴⁰ See Egloff, *supra* note 38, at 19.

event taking place over a longer time span.⁴¹ Many insurers were opposed to this perceived judicial trend, arguing that an “accident” needed to be an event confined in time and space.

During the 1955–1966 period, these insurers either changed their views, or accepted that this elongated judicial interpretation of the “accident” trigger of coverage was inevitable.⁴² In addition, some insurers offered occurrence-basis coverage, which was an attractive competing product because it clearly provided coverage for liability that resulted from ongoing conditions. In response, as part of the insurance industry’s 1966 revision to the standard CGL policy, the term “occurrence” was substituted for the term “accident,” with an “occurrence” being defined as “an accident, including injurious exposure to conditions, which results, during the policy period, in bodily injury or property damage neither expected nor intended from the standpoint of the insured.”⁴³ Regarding the 1966 Form, one attorney representing insurers commented:

⁴¹ See ROWLAND H. LONG, *THE LAW OF LIABILITY INSURANCE* §1.08, at 1-33, 1-36 – 1-37 (1997); ERIC MILLS HOLMES, *HOLMES’ APPLEMAN ON INSURANCE* § 117-3, at 274–76 (2d ed. 1981). Compare *Jackson v. Employers’ Liab. Assur. Corp.*, 248 N.Y.S. 207, 210 (N.Y. Sup. Ct. 1931), *aff’d*, 259 N.Y. 559 (N.Y. 1932) (holding that an “accident” must be confined in time and space), with *Hauenstein v. St. Paul-Mercury Indem. Co.*, 65 N.W.2d 122, 126 (Minn. 1954), and *Shipman v. Emp’rs Mut. Liab. Ins. Co.*, 125 S.E.2d 72 (Ga. Ct. App. 1962) (holding that an “accident” may take place over time). *Hauenstein*, a “property damage” case under the CGL, would have come out differently today because the 1966 form changed the definition of the term “accident” to require “physical” injury (not economic injury alone). However, the *Hauenstein* analysis regarding the term “accident” remains reflective of the emerging majority view of the time.

⁴² See, e.g., John J. Tarpey, *The New Comprehensive Policy: Some of the Changes*, 33 INS. COUNS. J. 223, 223 (1966) (“The principal reason given for revision of the policies [from the 1955 form to the 1966 form] was adverse court decisions.”). Tarpey was a partner in the New York-based law firm LeBoeuf, Lamb & Leiby (which subsequently became LeBoeuf, Lamb & Leiby, a firm that continued to represent insurers in coverage matters, which then merged with the Dewey Ballentine Firm prior to the ultimate demise of Dewey LeBoeuf in 2012 due to financial difficulties). He was also a member of the Federation of Insurance Counsel. *Id.*

⁴³ BRITTON D. WEIMER, *CGL POLICY HANDBOOK* § 3.01[A], at 3-3 (2nd ed. 2012).

Probably the most significant portion of the definition [of “occurrence”] is the phrase “during the policy period”. . . . This should remove problems of interpretation where causative factors operate over a long period of time before any harm results and also where the negligent act or the operative legal fact is far removed in time from the happening of the injury (e.g., a defect in manufacture, the sale of the product).⁴⁴

In other words, coverage was not only comprehensive for a given policy period, but insurers also accepted the risk of coverage for injuries taking place over multiple policy periods.⁴⁵

⁴⁴ Tarpey, *supra* note 42, at 224. The language of the 1966 form’s definition of “occurrence” also clarified what had long been the understanding of the insurance industry and the courts: the bodily injury or property damage caused by an accident/occurrence must produce injury or damage “during the policy period” in order to trigger coverage. If a policyholder was negligent (either episodically or chronically), but the negligence did not harm any third party during the policy period, there was no insured event and no trigger of coverage. If, however, this negligence produced injury in a later year, the occurrence basis CGL insurance applicable to the year of injury would be triggered and would respond to the claim. With the change from an “accident” policy to an “occurrence” policy, the focus of the trigger inquiry shifted from some uncertainty as to timing to a focus on the time at which the third party allegedly suffers injury due to actions for which the policyholder is legally liable. *Id.*

⁴⁵ See Gilbert L. Bean, New Comprehensive General and Automobile Program: The Effect on Manufacturing Risks 6 (Nov. 15–18, 1965) (unpublished paper) (“[C]overage no longer attaches when the accident occurs but rather when the injury or damage takes place. This means that the policy in force when a particular injury or damage takes place is the one which applies, regardless of when the causing accident took place.”). Bean was an executive with Liberty Mutual and one of the drafters of the 1966 CGL. *Id.* at 1; see also *id.* at 7 (noting possibility that events taking place long ago can trigger coverage in subsequent policy years if the injury from those events takes place during later policy years); Richard H. Elliot, *The New Comprehensive General Liability Policy*, in *LIABILITY INSURANCE DISPUTES* 12-3, 12-5 (Sol Schreiber ed., 1968) (“[F]or the purpose of applying coverage — the injury must take place during the policy period.”). Elliot was an insurance industry official. *Id.* at 12-3; Letter from E.W. Sawyer, Attorney, to Robert L. Mannon, Fireman’s Fund (June 8, 1939).

Under the majority of judicial decisions and what appears to be the majority view of the application of the “accident” trigger, the result would be the same: it was the injury, not the antecedent negligence or other liability-creating conduct that triggered the CGL policy. Accidents “in the air,” so to speak, did not trigger

In the 1973 revisions to the CGL form, there was also a technical modification to the “occurrence” and “bodily injury” terms of the policy.⁴⁶ Insurers understood that an occurrence trigger would potentially provide coverage for gradual, ongoing, or continuous injury. As one insurer representative put it, although “[i]n most cases, the injury will be simultaneous with the exposure,” in “some other cases, injuries will take place over a long period of time before they become manifest,” citing “[t]he slow ingestion of foreign matters and inhalation of noxious fumes” as examples. Thus, in “cases involving cumulative injuries, more than one policy contract may come into play in determining coverage and its extent under each policy.”⁴⁷

Using the examples of waste disposal and pollution, one commentator illustrated the operation of the occurrence basis trigger and its potential to result in triggering of multiple policies using pollution liability as an example, noting that “if the injury or damage from waste disposal should continue after

coverage. However, because in most instances, negligence and injury were nearly simultaneous (consider, for example, poor driving, a careless workman, or an exploding appliance), insurers were undoubtedly taken aback when the asbestos tort arrived. Because inhaled asbestos continues to inflict new damage, it had greater than ordinary potential to trigger multiple policies.

⁴⁶ As noted above, the 1966 CGL form stated that coverage was triggered by an “occurrence” causing bodily injury or property damage “during the policy period”. In 1973, this “during the policy period” language was relocated from the “occurrence” definition to the bodily injury definition. Beginning with the 1973 Form, “bodily injury” was defined as injury, sickness, or disease “sustained by any person which occurs during the policy period,” including resulting death. The relocation of this language was not intended to effect a substantive change in the meaning of the CGL. See ISO Memorandum from Richard H. Elliott, Vice President, Commercial Cas. Dep’t, to Dwight V. Strong, Chairman, WAIB-IBAC Comm. on Revised Liab. Forms 1 (Sept. 22, 1972) (excerpted in more detail in Stempel, *Assessing the Coverage Carnage*, *supra* note 27, at 366 n.40); Letter from Richard H. Elliot, Vice President, Commercial Cas. Dep’t, to Dwight V. Strong, Chairman, WAIB-IBAC Comm. on Revised Liab. Forms 1–3 (Sept. 22, 1972) (containing ISO comments regarding 1973 CGL Revision).

⁴⁷ See Norman Nachman, *The New Policy Provisions for General Liability Insurance*, 18 CPCU ANNALS 196, 199–200 (1965) (Nachman, was at the time, manager for non-automobile casualty insurance and multiple lines insurance at the National Bureau of Casualty Underwriters); see also Bean, *supra* note 45, at 2 (emphasizing that 1966 form is “considerably broader” in providing coverage for gradual injuries but emphasizing that “coverage, however, is still a casualty coverage . . .”).

the waste disposal ceased, as it usually does, it could produce losses on each side of a renewal date, and in fact over a period of years, with a separate policy applying each year.”⁴⁸ Further, because “[t]he policy limits are renewed every year, so the underwriter of a manufacturing risk may have his limits pyramid under this new contract.”⁴⁹

Without doubt, liability insurers understood that the shift from an accident trigger to an occurrence trigger constituted a “broadening of coverage”⁵⁰ even if they were not certain exactly how this new trigger arising out of gradual or ongoing conduct causing injury might play out in practice. Insurers realized that, because of the breadth of the CGL coverage commitment, they would need to control their exposure through other means such as the exclusion of specific risks⁵¹ (today referred to as “lasering out” particular risks) and the use of policy sub-limits for certain types of problematic liability.⁵² Regular review of policies and

⁴⁸ Bean, *supra* note 45.

⁴⁹ *Id.* As this commentator noted, insurers still retained significant protection in that “the new policy still gives the carrier the right to cancel a policy on 10 days notice.” *Id.* But although this “may free the carrier from liability for future injury or damage from a [sic] occurrence which has already taken place while he was on the risk,” this type of “cancellation would be no escape from consequences of mishaps which had already happened.” *Id.* at 7 (“I doubt very much whether the courts would permit a cancelling company to escape the inevitable consequences of what had already happened during their period of insurance.”).

⁵⁰ See Memorandum from R.H. Elliott, Secretary of the National Casualty Standards Bureau, to “Regional Vice Presidents,” Jan. 4, 1937, attaching Richard H. Elliott, The January 1, 1973 Changes in the Comprehensive General Liability Policy and in the General Liability Manuals, Address to Kansas State Association of Insurance Agents, Jan. 3, 1973, at 2.

⁵¹ See SAWYER, *supra* note 2, at 70 (“[T]here are situations in which it is necessary to exclude from the application of the policy certain business locations in their entirety or certain hazards at specific locations.”).

⁵² See *id.* at 71 (“If higher limits of liability are required for one hazard, such as elevators, the comprehensive policy may be written for the limits common to all hazards and the higher limits may be afforded by endorsement for elevators. If lower limits are required for one hazard than for the other hazards, the limits must be reduced for the single hazard. In either case the hazard which is to have different limits must be described in the endorsement in the same manner as it would be described in a schedule or single cover policy. If the limits for the

according adjustment of premiums or cancellation were also seen as important to controlling risk under the more comprehensive cover of the CGL form.⁵³

In addition, insurers were well aware that expanding the trigger of the industry's basic liability policy could expose insurers to more uncertain risk than that presented by other lines of insurance. Writing shortly before the 1966 revisions to the standard form CGL policy, insurance authorities noted:

The possible liability loss tends to be much more fluid and difficult to estimate than some other types of losses, such as property losses. Changing law and social outlook continually alter the size of judgments, mutations being obvious in the recent trend of verdicts in personal injury accidents. At the same time, it is virtually impossible to put a precise ceiling on a liability loss. Property may be insured for its value, but many forms of liability know no such easy limitations. The risk manager of a large pharmaceutical house admitted that its potential liability arising from products is virtually a matter of guesswork.

Finally, the liability peril not only involves a loss but may imply or seem to imply moral

hazard are to be reduced below the policy limits it is not necessary to bother with the exclusions, because all of the coverage for the hazard is comprehensive insurance.”). See also C.A. KULP, CASUALTY INSURANCE: ANALYSIS OF HAZARDS, POLICIES, COMPANIES AND RATES 38 (rev. ed. 1942) (“Liability forms have policy limits which are based essentially not on the amount of insurance required for full protection (which is incalculable) but on what the insured wishes to pay for. Soundly selected, the limits will cover all but the most unusual losses. These limits, however, apply per person and per accident not per year.”).

C.A. KULP, CASUALTY INSURANCE: AN ANALYSIS OF HAZARDS, POLICIES, COMPANIES AND RATES 38 (rev. ed. 1942)

⁵³ See SAWYER, *supra* note 2 (“In considering surveys and audits one cannot keep too closely in mind this feature of the comprehensive liability plan The success or failure of comprehensive liability insurance rests almost entirely upon the thoroughness with which the survey and audit are made.”); *id.* at 110 (providing example of discovery of additional hazards and risks after audit).

shortcoming of the party who is liable. Consider, for example, the doctor charged with malpractice, or the careless driver charged with liability for the death of a pedestrian, or the defendant charged with libel or slander or assault and battery. This aspect, too, may have important implications for any device to treat the liability risk.⁵⁴

In essence, liability insurers “knew” that by expanding to an occurrence trigger, they were increasing their own risk that liability losses would span more than one policy period and correspondingly increase their responsibility for losses such as toxic torts or pollution.⁵⁵ Certainly, insurers knew that by adopting an occurrence basis trigger, they could potentially be covering latent injury cases long after the initial exposure to the harmful substance and that they were accepting the risk of changing social and legal conditions as well as new knowledge regarding the dangers of certain products or substances.

The drafters of the CGL revisions may not have anticipated the large product liability claims and mass torts such as those involving asbestos or hazardous waste, but they clearly anticipated multiple policies being triggered by a liability hazard and knew that this risk was less predictable than many of the other risks they undertook. Insurers also knew that the design of the liability insurance product could affect the tort liability regime, in particular prompting wider recovery as judges and jurors became increasingly aware of the likely presence of at least some liability insurance for the defendant. It appears that

⁵⁴ See HERBERT S. DENENBERG ET AL., *RISK AND INSURANCE* 472 (2d ed. 1974). Accord, GREENE, *supra* note 14, at 289 (“[o]ne of the most serious financial risks covered by insurance is that of loss through legal liability for harm caused others.”); KULP, *supra* note 52, at 78 (liability insurance and legal regime closely linked).

⁵⁵ See Nachman, *supra* note 47, at 199–200; ROBERT I. MEHR & EMERSON CAMMACK, *PRINCIPLES OF INSURANCE* 340–41 (4th ed. 1966) (noting that term “accident” was sometimes not held to apply to injuries such as those “brought on by repeated exposures to dust from cement” but that term “occurrence” clearly applied to this type of injury and triggered coverage under a liability policy) (note, too, the similarity between an injury from cement dust and one resulting from asbestos dust).

insurers willingly embraced this risk in the pursuit of broader, more saleable coverage and corresponding profit.⁵⁶

II. THE SUCCESS OF THE CGL IN SPITE OF LIABILITY SHOCKS

Issues of mass tort and long tail liability have tended to dominate discussion of whether broad form coverage such as that favored by Elmer Sawyer and other industry leaders of the mid-twentieth century retains viability. In particular, the asbestos mass tort is often invoked as an example of the problems insurers face when attempting to write broad occurrence-based coverage.⁵⁷ Although coverage obligations

⁵⁶ See DONALD S. MALECKI & ARTHUR L. FLITNER, COMMERCIAL GENERAL LIABILITY 115–16 (8th ed. 2005).

⁵⁷ Insurers frequently worry that emerging liabilities could be the “next asbestos.” See Douglas J. Giuliano, Comment, *Mixed Dust Claims – The Next Asbestos, or Much Ado About Nothing?*, 1 FIU L. Rev. 107 (2006); Susanne Sclafane, *Homeowners Insurers Could be Named in Chinese Drywall Suits, Legal Expert Says; Lawyers predict ‘litigation explosion,’ but say drywall not the ‘next asbestos’*, National Underwriter (Prop. & Cas. Ed.), April 27, 2009. The concern arises because policies written with any breadth that do not specifically exclude coverage for a particular type of claim are at least potentially implicated in coverage for matters that may take years to resolve, or decades as did asbestos. See Special Project: *An Analysis of the Legal, Social, and Political Issues Raised by Asbestos Litigation*, 36 Vand. L. Rev. 573, 709–10 (1983):

The expansive asbestos litigation and corresponding liability of asbestos manufacturers pose grave problems for the insurance industry. . . . When the insurance industry drafted and negotiated the language in the insurance policies, the concept of latent diseases was virtually unknown. Also, at the time the policies were drafted, liability operated differently. Hence, policy language that requires a single injury is inappropriate for latent diseases such as asbestos-related illnesses. In addition, the available medical data cannot explain the exact causes or etiologies of the asbestos-related diseases. The lack of medical information concerning these diseases makes it difficult for courts to interpret the insurance clauses and delineate liability clearly.

Because writing policies that provided comprehensive coverage and accepted the risk of future medical and legal developments turned out badly for the insurance industry, many of its members have since been resistant to providing broad coverage, as reflected in fears over a possible “next asbestos” and continued remembrance of the problems posed by asbestos for insurers.

related to asbestos (along with pollution and product liability) has of course adversely impacted the profitability of liability insurance, it has hardly crippled the industry or the viability of the broad coverage/bundled risk business model. On the contrary, the manner in which insurers have weathered the asbestos storm — despite forty years of tort litigation and 35 years of major liability insurance coverage litigation — demonstrates the resilience of the comprehensive coverage ideal as serving both risk management and industry revenue goals.⁵⁸

See, e.g., In re Plant Insulation Co., 469 B.R. 843, 871 (Bkrtcy N.D. Cal. 2012) (“Asbestos claims present unique problems for courts and insurers” due to the long latency period before manifestation of asbestos-related disease, which is covered under the broad-based CGL policy, of which several governing years of policy periods may be applicable); Jennifer L. Biggs, *The Scope and Impact of Asbestos Litigation*, 44 S. Tex. L. Rev. 1045, 1047-55 (2003) (asbestos mass tort presented substantial litigation volume and risks of large awards against defendants that “hold insurance policies, so the increase in costs to defendants also leads to an increase in costs to insurers and reinsurers.”) (also noting second wave of asbestos claims and coverage litigation in early twenty-first century, as well as initial wave during 1980s, each implicating insurance coverage of broadly written standard CGL form). *See also id.* at 1071 (“the United States insurance industry, through year-end 2001, had paid \$23.5 billion and was holding \$13 billion in reserves for asbestos claims.”); Ben Berkowitz, *The Long, Lethal Shadow of Asbestos*, National Underwriter (Prop. & Cas. Ed.), May 11, 2012) (asbestos claims and corresponding insurance coverage issues continuing apace “[h]alf a century after the first wave of lawsuits were filed for illnesses linked to exposure to asbestos and 40 years after new regulation sharply curtailed use of the insulating and fire-resistant mineral;” “when insurers AIG and The Hartford announced additions of \$1.3 billion and \$290 million, respectively, to their asbestos reserves, the companies blamed tertiary defendants that never anticipated litigation and now are being sued;” insurers continually underestimate ultimate insurance losses because of continued flow of new cases raising potential for coverage.).

When insurers finally realized the scope of the asbestos exposure they faced, the industry excluded coverage in the 1986 revisions to the CGL form. Chastened by the asbestos experience, insurers since 1986 have moved quickly to exclude coverage for specific types of emerging claims such as toxic mold and Year 2000 computer conversion problems in a manner inconsistent with the comprehensive approach to insurance reflected in the CGL policy as envisioned by Elmer Sawyer.

⁵⁸ *See Asbestos Loss Estimate Raised to \$85bn*, REACTIONS, Jan. 29, 2013, at 8; *see also* Mark E. Ruquet, *Overall Asbestos Losses to Rise to \$85B*, PROPERTY CASUALTY 360: NAT’L UNDERWRITER (Dec. 18, 2012), <http://www.propertycasualty360.com/2012/12/18/overall-asbestos-losses-to-rise-to-85b> (noting industry’s asbestos losses of \$2 billion per year).

Notwithstanding the magnitude of the asbestos mass tort, CGL insurers survived and have generally profited most years despite the ongoing asbestos liabilities. Even a severe tort exposure such as asbestos has significant traits tending to advantage insurers, as do many other significant liability coverage exposures. Adjudication and payment of claims has extended over decades, postponing payment. As has been noted in the past, “this allows insurers to garner years of investment income and to pay claims in dollars whose real value has been substantially reduced by inflation.”⁵⁹ By contrast, property insurers must usually pay covered claims within a relatively short time frame after receipt of premiums. The property insurer thus gets far less benefit from either investment income or the effects of inflation. And the perception that insurers are put upon because of claims may help insurers procure favorable judicial decisions that are perceived as mitigating their pain or equalizing previous favorable decisions for policyholders.⁶⁰

The asbestos and pollution mass torts also enabled insurers to structure products and operations in a manner that reduced future exposure;⁶¹ a response, of course, suggesting that fragmenting risk may in time be necessary in order to protect the viability of a bundled insurance product. However, it is

⁵⁹ Stempel, *Assessing the Coverage Carnage*, *supra* note 27, at 351.

⁶⁰ See *id.* at 351, 443, 463–64; Mike Tsikoudakis & Sarah Veysey, *AIG, Marsh Formalize Seven-day Pledge to Pay Big Claims*, *BUS. INS.*, Mar. 11, 2013, at 10 (describing announced commitment by AIG Group and Marsh to “quickly pay multimillion dollar commercial property damage claims”); Michael Adams, *Florida Senate to Unveil Property Insurance Reforms*, *INS. J.* (Feb. 1, 2013), available at <http://www.insurancejournal.com/news/southeast/2013/01/31> (noting political dissatisfaction with dominance of Citizens Property Ins. Corp. for windstorm policies when insurer was intended to be only a backstop to the private market, a problem in part owing to the unattractiveness of insuring first-party property damage windstorm exposures).

⁶¹ See Stempel, *Assessing the Coverage Carnage*, *supra* note 27, at 351–53 & n.7, 363–68 & n.36, 443–44, 464, 467 (describing degree to which CGL insurers became more sophisticated in protecting themselves as a result of lessons learned from the asbestos mass tort. Also describing the degree to which asbestos-related liability may have played a role in courts adopting doctrine more favorable to insurers, such as pro-ratio of responsibility of consecutively triggered liability policies, not withstanding “all sums” language of insuring agreement or expansive construction of pollution exclusion).

useful to consider what might have happened if the asbestos mass tort had not fallen largely upon the CGL form but instead had been borne by a more specialized policy (e.g., a product liability only policy, a toxic tort policy, an insulation contractor's operations liability policy). In such a case, the insurer underwriting such a specialized insurer would surely have fared far worse than CGL underwriters who had earned premiums on "winning" exposures such as slip-and-falls or garden variety products claims sufficient to withstand the onslaught of losing asbestos claims.

Today, some risks such as pollution liability have been removed from the CGL form but are still subject to coverage in a more specialized policy. But these more specialized environmental impairment policies offer coverage only under much more limited terms than were available under the pre-1986 CGL form (e.g., claims-made format, tight temporal discovery and reporting requirements, lower limits, higher deductibles, higher premiums). It is a shadow of the hazardous waste coverage once offered by the CGL.⁶²

Had insurers elected to keep such coverage in the comprehensive policy (using sub-limits, a co-pay or higher retention, language akin to the former qualified pollution exclusion or additional premiums), the risk-spreading impact of

⁶² APPLEMAN ON INSURANCE §193 (describing evolution of pollution coverage under standard CGL policy and specialized environmental liability coverage that has emerged in the wake of restrictions on pollution coverage in the CGL policy); KENNETH S. ABRAHAM, ENVIRONMENTAL LIABILITY INSURANCE LAW: AN ANALYSIS OF TOXIC TORT AND HAZARDOUS WASTE INSURANCE COVERAGE ISSUES (1991) (providing overview of pollution coverage and exclusions in general liability insurance and more specialized liability insurance); KENNETH S. ABRAHAM, DISTRIBUTING RISK: INSURANCE, LEGAL THEORY, AND PUBLIC POLICY (1986) (same, arguing to a degree that judicial willingness to provide pro-policyholder construction of pre-1986 general liability insurance prompted insurers to restrict pollution coverage in the CGL policy, resulting in less coverage than would have been available under older policy forms construed more favorably to insurers). *See also* MARK S. DORFMAN, INTRODUCTION TO RISK MANAGEMENT AND INSURANCE 381-86 (8th ed. 2005) (describing insurer concern about providing broad pollution liability coverage and use of EIL policies as an alternative, noting that EIL policies use the more restrictive claims-made format less useful to policyholders). Professor Dorfman noted the potentially large size of pollution liability but failed to note that in the marketplace, EIL coverage is seldom available in the large policy limits found for CGL coverage).

bundling might have enabled general liability insurers to continue to offer pollution coverage in an format more useful to policyholders, using more restrictive policies only for high pollution risks rather than creating a situation in which many policyholders presenting only mild pollution risks undoubtedly forgo EIL insurance because of the cost and limited coverage. Potentially, insurers could have continued to capture premium dollars by continuing to offer pollution coverage of some type in the CGL without imperiling their risk pool

Whatever the scope of the basic property or liability policy, notable torts and natural disasters aid the ultimate bottom line of insurers by serving as advertisements for the product. After a large loss event, the public (both commercial and individual), is awakened to its need for insurance, tends to buy more of it (both higher limits and broader coverage to the extent available) and is willing to pay higher premiums for it. The losses of one bad year are often recouped within a fairly short time thereafter as individuals purchase more insurance in response to a heightened awareness of catastrophic risk.⁶³

Although some claims are commonly thought to be insufficiently fortuitous to be insurable, actual insurer operations belie this fact. For example, the purchase of new

⁶³ See Report: *Louisiana Homeowners Insurance Rates Rising More Slowly*, INS. J. (Jan. 16, 2012), <http://www.insurancejournal.com/news/southcentral/2012/01/16/231255.htm> (describing increase in homeowners' insurance rates following Hurricane Katrina); see also Todd Wallack, *2011 Storms Trigger Home Insurance Rate Hikes: Increases as High as 20 Percent Proposed*, BOS. GLOBE, Mar. 4, 2012, http://www.boston.com/business/personalfinance/articles/2012/03/04/2011_storms_trigger_home_insurance_rate_hikes/?page=1 (describing proposed increases in homeowners' insurance rates in Massachusetts following a year that brought tornadoes, severe snowstorms, and Tropical Storm Irene); see also Lynn Cowan, *After Storms, Insurers' Stock Sales Swell to Shore Up Balance Sheets*, WALL ST. J., Dec. 12, 2005, <http://online.wsj.com/news/articles/SB113435159003019836> (describing insurance company stock sales after hurricanes to "shore up their balance sheets as the claims come marching in."); see also HOWARD C. KUNREUTHER ET AL., AT WAR WITH THE WEATHER: MANAGING LARGE-SCALE RISK IN A NEW ERA OF CATASTROPHES 87 (2009) (describing increase in flood insurance policies following major floods and Hurricane Katrina); Howard Kunreuther & Mark Pauly, *Rules Rather Than Discretion: Lessons from Hurricane Katrina*, 33 J. RISK UNCERTAINTY 101, 106–07 (2006) (describing relationship between consumers' past experience with severe weather with their subsequent insurance purchases).

insurance is viewed as unavailable after a loss event, though this is not necessarily true. So long as there remains some element of uncertainty, insurers can continue to offer profitable policies. Consequently, even in the aftermath of a disaster, insurers can make profitable sales of policies related to the catastrophe.

For example, after the MGM Grand Hotel Fire of 1980, MGM purchased an after-the-fact CGL policy.⁶⁴ The policy agreed to defend and settle claims in return for a premium, one that obviously increased over what would have been charged in the absence of the fire because there was no uncertainty about the risk of an occurrence of fire (it had of course already happened) and the hotel's clear liability (as an innkeeper it was essentially strictly liable under prevailing law). But there remained plenty of uncertainty as to the ultimate net aggregate tally of damages and the amount of claims adjustment expenses required to manage the litigation. Rather than continue to manage this risk based on its package of policies purchased before the fire and its own resources, the hotel shifted this risk to a liability insurer that was happy to be paid for accepting the risks posed by the litigation.⁶⁵ In essence, the insurer calculated that it could invest the premium payment wisely enough to earn more than it would pay out in claims and administrative costs, including defense costs.

A related and more recent example of the insurance industry's ability to profit even when accepting a large pool of risk is provided by famed investor Warren Buffet and insurers owned by Buffet's Berkshire Hathaway company.⁶⁶ They agreed to take over management of asbestos claims for other insurers or reinsurers on those risks.⁶⁷ In essence, Berkshire acquired

⁶⁴ In re MGM Grand Hotel Fire Litig., 570 F. Supp. 913, 915, 928 (D. Nev. 1983).

⁶⁵ See *id.* at 928–29.

⁶⁶ See RICHARD J. CONNORS, WARREN BUFFETT ON BUSINESS: PRINCIPLES FROM THE SAGE OF OMAHA 71-76 (2010) (chapter on “The Assessment and Management of Risk”).

⁶⁷ See Erik Holm, *AIG Unloads Asbestos Liabilities; Buffett Gets 'Float'*, WALL ST. J., Apr. 21, 2011, 12:01 AM, <http://online.wsj.com/article/SB10001424052748704658704576274662791668194.html> (describing Berkshire asbestos liability transactions with AIG, Equitas, and CNA Financial Corp).

billions of dollars in reserves held by these insurers (and the ability to have them invested by Buffet) and can profit from the arrangement even though it faces thousands of asbestos-related claims. To be sure, Buffett is making a pretty big bet in favor of his team's ability to resolve claims at a lower cost than what others had anticipated and on his ability to earn adequate returns on the acquired reserves.⁶⁸ And recent reports suggest that the arrangement may not be working as well as originally anticipated.⁶⁹ But if the insurers can come late to the asbestos mass tort and still make money, they can probably provide more inclusive, less fragmented insurance products and make money.

In addition to assisting insurers in selling more coverage in return for larger premiums, the CGL policy to some degree saved policyholders from themselves, by forcing them to purchase broader coverage that they probably should have, but might be unlikely to purchase if shopping around (even with the aid of an agent or broker), and selecting among an array of products. Even fairly experienced or sophisticated policyholders aided by intermediaries could miss something and have gaps in coverage that would come back to haunt them in later years when liability-producing events occur.

A collateral benefit that appears not to have been part of the Sawyer agenda was the availability of more resources for

⁶⁸ Buffett himself has acknowledged this. See Andrew Frye, *Warren Buffett's Insurance Growth Engine May Stall*, BLOOMBERG (Mar. 2, 2012, 7:16 AM), <http://www.bloomberg.com/news/2012-03-02/buffett-s-insurance-engine-of-growth-set-to-stall.html>; Letter from Warren E. Buffett, Chairman of the Bd., Berkshire Hathaway Inc., to the Shareholders of Berkshire Hathaway Inc. 7 (March 1, 2013), available at <http://www.berkshirehathaway.com/letters/2012ltr.pdf> ("If our premiums exceed the total of our expenses and eventual losses, we register an underwriting profit that adds to the investment income our float produces. When such a profit is earned, we enjoy the use of free money — and, better yet, get *paid* for holding it. That's like your taking out a loan and having the bank pay *you* interest.").

⁶⁹ See Erik Holm, *Insurers May Face \$11 Billion More in Asbestos Claims*, WALL ST. J., Dec. 17, 2012, 10:27 AM, <http://online.wsj.com/article/SB10001424127887324907204578185224076122106.html> (discussing how asbestos claims costs to date are proving higher than anticipated and investment returns are less than anticipated); see also Ben Berkowitz, *Analysis: New Asbestos Charges Point to Reserve Woes*, REUTERS (July 28, 2011, 11:07 AM), <http://www.reuters.com/article/2011/07/28/us-insurance-asbestos-idUSTRE76R4CW20110728>.

compensating tort victims. The liability revolution of the twentieth century probably would not have taken place without the greater amount of insurance becoming available.⁷⁰ This exerted at least some hydraulic pressure on the judicial system to expand liability⁷¹ and increase damage awards to tort

⁷⁰ See KENNETH S. ABRAHAM, *THE LIABILITY CENTURY: INSURANCE AND TORT LAW FROM THE PROGRESSIVE ERA TO 9/11*, at 4–5 (2008); Tom Baker, *Liability Insurance as Tort Regulation: Six Ways That Liability Insurance Shapes Tort Law in Action*, 12 CONN. INS. L.J. 1, 3–4 (2005); see also Adam F. Scales, *The Chicken and The Egg: Kenneth S. Abraham's "The Liability Century,"* 94 VA. L. REV. 1259, 1259–60 (2008) (book review of ABRAHAM, *supra*).

⁷¹ Or at least to relax or remove barriers to greater recovery. The judiciary arguably created new rights of recovery or causes of action in cases like *Escola v. Coca-Cola*, 150 P.2d 436, 463 (Cal. 1944) (imposing strict liability on manufacturer rather than requiring claimant to prove negligence in the product's manufacture or design); *Ybarra v. Spangard*, 154 P.2d 687, 689–92 (Cal. 1944) (applying doctrine of *res ipsa loquitur* to permit recovery by patient, when medical equipment was left in body after surgery, without imposing burden of proving negligence or proffering expert testimony); *Dillon v. Legg*, 441 P.2d 912, 925 (Cal. 1968) (permitting family member to recover for emotional distress after seeing loved one killed, even though family member was not physically in danger).

But in many instances, tort liability expanded, not because of new causes of action, but because of relaxation or elimination of defenses to such claims. For example, courts gradually restricted or eliminated the fellow servant rule, assumption of risk, and intra-family immunity. Similarly, courts and legislatures moved away from a pure contributory negligence regime (in which any negligence by a claimant precluded recovery) to one of comparative negligence, most commonly modified comparative negligence in which the claimant was permitted to recover so long as its negligence was not greater than that of the tortfeasor. Through a variety of developments, tort liability and the reach of tort law expanded significantly from the 1940 until at least the 1980s and arguably through the end of the twentieth century. See Anita Bernstein, *The 2x2 Matrix of Tort Reform's Distributions*, 60 DEPAUL L. REV. 273, 280–282 (2011) (analyzing the tort reform movement of the late twentieth century as an attempt to curtail perceived overbroad expansion of tort law during much of the century). See generally DAN B. DOBBS & PAUL T. HAYDEN, *TORTS AND COMPENSATION: PERSONAL ACCOUNTABILITY AND SOCIAL RESPONSIBILITY FOR INJURY* (5th ed. 2005); G. EDWARD WHITE, *TORT LAW IN AMERICA: AN INTELLECTUAL HISTORY* 3 (2003); VICTOR E. SCHWARTZ ET AL., *PROSSER, WADE AND SCHWARTZ'S TORTS: CASES AND MATERIALS* (10th ed. 2000); W. PAGE KEETON ET AL., *PROSSER & KEETON ON THE LAW OF TORTS* (5th ed. 1984); Stephen D. Sugarman, *A Century of Change in Personal Injury Law*, 88 CAL. L. REV. 2403 (2000); Gary T. Schwartz, *The Beginning and the Possible End of the Rise of Modern American Tort Law*, 21 GA. L. REV. 601, 605–09 (1992) (all noting the

victims.⁷² And when these victims sought to collect, tortfeasors that might otherwise be impecunious were able to pay (without liquidating portions of their business) and continue on with their work (without seeking bankruptcy protection).

In short, the CGL really does appear to have been a win-win situation for affected constituencies. Insurers made money. Policyholders obtained greater protection and more effective risk management. Injured claimants received more compensation. Claims processing and litigation also appear to have become more efficient through an expanded duty to defend with reduced “Alphonse vs. Gaston” finger-pointing between insurers arguing over which specific policy covered the risk at issue in the lawsuit.⁷³ In addition, through the use of panel counsel and aggregate claims information, insurers became quite efficient at defending claims and resolving disputes, almost certainly more so than most of their policyholders.⁷⁴

expansion of tort liability during the mid-to-late-twentieth century, with some backlash or contraction emerging in the last decade or so of the century).

⁷² Even where there was not an expansion of liability or removal of defenses, courts gradually broadened receipt of evidence related to damages and permitted higher jury awards to stand. *See generally* 2 JACK B. WEINSTEIN ET AL., WEINSTEIN’S EVIDENCE: COMMENTARY ON RULES OF EVIDENCE FOR THE UNITED STATES COURTS AND STATES COURTS (1975) (first volume of influential multi-volume treatise published nearly contemporaneously with issuance of new Federal Rules of Evidence, which took broad view of admissibility); 1 GEORGE E. DIX ET AL., MCCORMICK ON EVIDENCE § 11, at 69 (Kenneth S. Broun ed., 7th ed. 2013) (describing the “gradual relaxation of the admissibility standard” for opinion evidence); 22 CHARLES ALAN WRIGHT & KENNETH W. GRAHAM, JR., FEDERAL PRACTICE AND PROCEDURE: EVIDENCE § 5177, at 893 (2012) (“Courts have embraced a number of doctrines, legitimate and illegitimate, to expand the admissibility of evidence beyond the narrow confines of Rule 401 relevance.”). Some even permitted courts to use additur to increase jury awards that were viewed as too stingy to claimants. *See, e.g.*, *Genzel v. Halvorson*, 80 N.W.2d 854, 859 (Minn. 1957).

⁷³ *See* Egloff, *supra* note 38, at 19 (discussing assessment of Travelers vice-president John Egloff); *see also* *State v. Brown*, 781 N.W.2d 244, 245 n.1 (Wis. App. 2010) (discussing the metaphor of Alphonse and Gaston, two once-popular cartoon characters engaged in a running joke of each waiting over-politely for the other to proceed through a door, resulting in neither making any progress through the door).

⁷⁴ The insurer efficiency is not without some drawbacks for lawyers, who often complain that insurance defense practice has become commodified and

This assessment of the CGL policy may be too sanguine for the tastes of many. Certainly, it clashes with the public relations narrative of the insurance industry,⁷⁵ a story that emphasizes the tough nature of the business and paints liability insurers as embattled guardians of sanity in a world dominated by the “litigation explosion,”⁷⁶ “jackpot justice,”⁷⁷ “junk science,”⁷⁸ law-

less financially rewarding as well as more difficult by insurer-dictated rules, some of which encroach upon lawyer professional autonomy and effective representation of the defendant policyholder. *See generally* Herbert M. Kritzer, *The Commodification of Insurance Defense Practice*, 59 VAND. L. REV. 2053 (2006); *see, e.g., In re the Rules of Prof'l Conduct and Insurer Imposed Billing Rules and Procedures*, 2 P.3d 806, 815 (Mont. 2000) (finding litigation guidelines of insurer interfered too greatly with defense attorney's professional responsibilities). Worse yet, some insurers appear to have adopted an overly resistant attitude toward claims resolution, resulting in unnecessary trials and unduly protracted litigation, with much of the cost externalized to the judicial system and society even if the strategy is effective for insurers seeking to reduce settlement payments. *See, e.g.,* Douglas R. Richmond, *Defining and Confining Institutional Bad Faith in Insurance*, 46 TORT TRIAL & INS. PRAC. L.J. 1 (2010) (describing excessively sharp practices of major disability insurer).

⁷⁵ Since the 1950s, and with renewed emphasis since the 1980s, insurers and potential business defendants have funded a fairly aggressive and wide-ranging advertising and public relations campaign portraying the tort system as excessively favorable to plaintiffs and unfair to businesses. *See* VALERIE P. HANS, BUSINESS ON TRIAL: THE CIVIL JURY AND CORPORATE RESPONSIBILITY 70–75 (2000); Stephen Daniels & Joanne Martin, “*The Impact That It Has Had Is Between People's Ears:*” *Tort Reform, Mass Culture, and Plaintiffs' Lawyers*, 50 DEPAUL L. REV. 453, 459 (2000); Edith Greene et al., *Jurors' Attitudes About Civil Litigation and the Size of Damage Awards*, 40 AM. U. L. REV. 805, 805–08 (1991); Elizabeth Loftus, *Insurance Advertising and Jury Attitudes*, A.B.A.J. 68 (Jan. 1979).

⁷⁶ The “litigation explosion” is a favored term of those criticizing the tort system as excessively claimant-friendly and hostile to business. As of July 25, 2013, the term appears in more than 2000 articles in the LexisNexis database of legal periodicals, a testament to its status as part of the lexicon of public policy discussions about American liability law. *See, e.g.,* Marc Galanter, *The Day After the Litigation Explosion*, 65 MD. L. REV. 3, (examining claims of litigation explosion and finding them empirically overstated in spite of widespread acceptance of concept by public); Jeffrey W. Stempel, *A Distorted Mirror: The Supreme Court's Shimmering View of Summary Judgment, Directed Verdict, and the Adjudication Process*, 49 OHIO ST. L.J. 95, 95–97 (1988) (noting popularity of term and concept and suggesting that fears of a litigation explosion have fueled support for unwise developments in civil procedure doctrine).

⁷⁷ Although less common than the term “litigation explosion,” the pejorative “jackpot justice” is widespread (cited in more than 120 articles in the LexisNexis database as of July 25, 2013). It refers to the notion that by submitting a claim to a jury, plaintiffs are engaging in something akin to gambling in which for a relatively modest investment in disputing costs they may reap a huge award, particularly if able to achieve punitive damages. This narrative is flawed, of course, in that punitive damage awards are relatively rare and seldom very large. See Anthony J. Sebok, *Punitive Damages: From Myth to Theory*, 92 IOWA L. REV. 957, 970–71 (2007) (“The empirical data shows that under none of these tests have punitive damages been acting in a way that one could describe as out of control. Studies in the 1980s and 1990s placed the median for punitive-damages awards between \$38,000 and \$52,000 per award. The mean awards were, of course, very different from the median. For example, according to the Department of Justice study, the median punitive-damages award in 1992 was \$50,000, and the mean award was \$735,000. This illustrates the effect of the rare multi-million dollar award—in that study, the mean was so high because of a handful of extremely high awards. In fact, although the mean was \$735,000, more than 75% of all the punitive-damages awards were less than 2/3 that value (e.g., less than \$250,000).” (footnotes omitted)); Robert J. Rhee, *A Financial Economic Theory of Punitive Damages*, 111 MICH. L. REV. 33, 48–49 (2012) (“The leading empirical scholars in this field, Theodore Eisenberg and his coauthors chief among them, have shown that: (1) punitive damages are infrequently awarded, (2) the amount of punitive damages is highly correlated to the amount of compensatory damages, (3) the median ratio of punitive to compensatory damages is less than 1.0, and (4) punitive damages are most likely to be awarded for intentional torts and economic wrongs. The empirical evidence shows that punitive damages are infrequent, stable, and predictable, and that the myth of out-of-control punitive damages is ‘groundless.’” (footnotes omitted)).

⁷⁸ See PETER W. HUBER, *GALILEO’S REVENGE: JUNK SCIENCE IN THE COURTROOM* (1991). Huber, a fellow at the conservative, pro-business Manhattan Institute coined or at least popularized the term and is perhaps the most prominent of a number of commentators who argued that, during the 1980s and 1990s, courts had become too receptive to weak or even unfounded expert testimony proffered by tort plaintiffs. See D. Michael Risinger, *Navigating Expert Reliability: Are Criminal Standards of Certainty Being Left on the Dock?*, 64 ALB. L. REV. 99, 101–03 (2000) (noting Huber’s successful intellectual entrepreneurialism with the term); see also Bert Black, *A Unified Theory of Scientific Evidence*, 56 FORDHAM L. REV. 595, 604 (1988) (arguing, as had Huber, that evidence rules were too lax and permitted too much receipt of baseless expert witness testimony supporting plaintiff claims). These arguments efforts bore some significant fruit in *Daubert v. Merrill-Dow Pharm.*, 509 U.S. 579, 592–97 (1993), in which the Supreme Court imposed significant new requirements for admission of expert testimony and emphasized the role of the judge as a “gatekeeper.”

suit “lotteries,”⁷⁹ and “judicial hellholes.”⁸⁰ This tale of woe trumpeted by defendants and insurers is overstated.⁸¹ But even if it were completely true as an indictment of the tort system or the inefficiency of civil litigation, it does not undermine the success of the CGL’s bundled approach or the wisdom of consolidated coverage generally.

Without a doubt, expanded liability such as product liability claims, including claims involving prescription drugs and medical devices, increased the exposure of many defendants and their liability insurers during the second half of the twentieth century. Hazardous waste claims put additional pressure on liability insurers. And then there was asbestos — the greatest mass tort in history. Nonetheless, these challenges to the insurance industry are independent of the issue of fragmented-versus-consolidated coverage. Regardless of whether a defendant’s liability insurance was in the form of a specific policy or in the broader form of the CGL policy, the claims would have been made and required defense and payment of successful claims and settlements. Similarly, there would likely have been coverage litigation of issues, such as trigger of coverage and allocation of the responsibility, of multiple insurers regardless of whether the policies at issue were broad or narrow in scope.

⁷⁹ A cousin of the term jackpot justice, the words “lawsuit lottery” appears in more than 150 legal periodicals in the LexisNexis database as of July 25, 2013.

⁸⁰ See *California Replaces Philly Atop “Judicial Hellholes®” List, joined by Jurisdictions in West Virginia, Illinois, New York and Maryland*, ATRA (Dec. 13, 2012), available at <http://www.atra.org/newsroom/california-replaces-reforming-philly-atop-judicial-hellholes-%C2%AE-list-joined-jurisdictions>. The moniker “judicial hellhole” is applied by critics of the tort system to particular jurisdictions perceived to be unduly friendly to plaintiff claims or hostile to business. It appears in nearly 300 law review articles in the LexisNexis database (as of July 25, 2013) and has been popularized by the American Tort Reform Association (ATRA), which publishes an annual list of its perceived worst ten such jurisdictions.

⁸¹ Much scholarly literature makes a strong case that claims of excessive litigation or undue judicial support of plaintiffs is overstated. See Marc Galanter, *Reading the Landscape of Disputes: What We Know and Don’t Know (and Think We Know) About Our Allegedly Contentious and Litigious Society*, 31 UCLA L. REV. 4 (1983).

If liability insurers stuck with the pre-CGL model, the problems exposed by the liability century would not have been resolved. Rather, they would have been focused on a few particular lines of the specific insurance products that previously dominated the field, including Owners, Landlords & Tenants insurance or Public Liability insurance. This hardly would have made the pollution and asbestos “crises” any better, and may have made them much worse. CGL insurers were able to weather the storms of these claims, in part because, the inclusiveness of the CGL worked as a marketing and sales device. This provided insurers with more premium dollars, much of which were held during boom years for stock market and real estate investment, giving CGL insurers vast resources with which to defend, resolve, and pay tort claims — including the troublesome pollution and asbestos claims. The same was true of the reinsurers that backstopped the CGL carriers. Without the benefits of CGL aggregation, particular insurers, most saddled with such claims, might not have showed the resilience of the CGL insurers.⁸²

⁸² See Stempel, *Assessing the Coverage Carnage*, *supra* note 27, at 417 (estimating that asbestos coverage liability is only a three percent drag on insurer earnings). The business moves of Berkshire Hathaway and Warren Buffet, acquiring books of business with substantial asbestos exposure in order to obtain their money for investing is consistent with the view that the asbestos coverage problem, although significant, has hardly been fatal for insurers. *Accord*, *Overall Asbestos Losses Reach \$85 Billion*, 360 ESSENTIALS, Jan. 2013, at 10. Although \$85 billion is, of course, a lot of money, this is the estimated total liability of insurers stemming from asbestos claims that began during the 1960s. After nearly 50 years, this amounts to less than \$2 billion per year during a period when liability insurers regularly wrote hundreds of billions of dollars in premiums and amassed surplus and reserves of similar magnitude.

See also Sean M. Fitzpatrick, *Fear Is the Key: A Behavioral Guide to Underwriting Cycles*, 10 CONN. INS. L.J. 255, 260 (2004) (“[I]nsurers repeatedly rob the Peter of their present risk pool to pay the Paul of some prior year’s pool whose premiums turned out to be insufficient to fund its liabilities. This process also works in reverse, of course, when insurers’ actual experience is more favorable than anticipated, allowing them to release excess reserves to offset poor results experienced in later periods - robbing Paul to pay Peter in this instance.”); Howard Kunreuther & Mark Pauly, *Insurance: The Most Misunderstood Industry*, KNOWLEDGE@WHARTON, Feb. 13, 2013, available at <http://knowledgetoday.whartonupenn.edu/2013/02-insurance-the-most-misunderstood-industry> (“Insurance firms also behave strangely. After they suffer a severe loss, they may decide that a risk is completely uninsurable rather than determining whether they should increase their premium. For example,

Despite the blows of asbestos and other liability events, CGL insurers remain in good health. As institutional repeat players, CGL insurers were able to absorb the blows while simultaneously taking steps to reduce the risk of such losses in the future. In response to the tort upsurge, CGL insurers added an asbestos exclusion, pollution exclusions, aggregate limits, and other coverage-narrowing devices. These included adoption of a claims-made approach to product liability or the separate environmental impairment policies that are now offered separately because pollution coverage is no longer available under the CGL form.

To be sure, some of these protective reactions in the CGL form are at odds with the inclusive approach. However, they hardly make the CGL into a Swiss cheese policy, as long as the curtailments of coverage are relatively few in number, clearly demarcated, and expressed in relatively clear, unhidden prose. The standard CGL can better be described as an insurance product that now has a few mass tort holes born of experience, but still provides generally comprehensive coverage. Even in its modified form after the 1986 changes and influence from mass torts, the CGL policy provides better protection for policyholders than the smorgasbord of separate liability policies that it replaced. And, as always, insurers charge higher premiums when they offer more coverage, resulting in more investment income. Compared to a return to more fragmented general liability coverage, the CGL continues to be a success preferable to the alternatives.

The liability insurance industry itself has demonstrated that it is able to continue to use the CGL form as a prime means of underwriting general liability risk. Most obviously, the CGL remains offered to policyholders. Although the market may occasionally experience “hard” periods of higher premiums, restricted availability, and lower policy limits, the CGL remains widely available at prices policyholders are willing to pay.

Furthermore, the dominant form of CGL remains an occurrence-basis policy that policyholders generally prefer because it shifts more risk to the insurer. In the mid-1980s,

prior to 9/11, insurers did not price terrorism risk when providing coverage against damage to commercial property. After 9/11, most carriers refused to offer terrorism insurance because they feared catastrophic losses from future attacks.”).

liability insurers sought to expand use of the claims-made CGL, perhaps even using it to completely supplant the occurrence-basis form.⁸³ The effort, however, faltered and today the typical CGL sold is an occurrence policy. Insurers responded to the preferences of the policyholder market by continuing to offer a broader form of coverage that has been sought out by sufficiently important customers, rather than shrinking or fragmenting coverage.⁸⁴

Another example of the continued viability of the inclusive CGL is provided by the risk in construction defect claims in the late twentieth century. As the saying goes, they “don’t build ‘em like they used to.” Booming but frequently defective construction, particularly in the Southern and Southwestern United States, led to an increase in construction defect litigation, sometimes aided as well by legislation and judicial rulings favorable to homeowners. This in turn led to rounds of coverage litigation as CGL insurers frequently interposed coverage defenses based on business risk exclusions such as the expected or intended injury defense, the “your work” exclusion, the “your property” exclusion and the like.⁸⁵

⁸³ See *Hartford Fire Ins. Co. v. California*, 509 U.S. 764, 795 (1993) (finding that state attorneys general may proceed in action alleging conspiracy by insurers to impose claims-made forms on policyholders in lieu of historically dominant occurrence-basis form).

⁸⁴ See *O’Shaughnessy v. Smuckler Corp.*, 543 N.W.2d 99 (Minn. Ct. App. 1996) (describing how in reaction to policyholder community opposition, liability insurers restored substantial coverage by adding a subcontractor exception to the CGL policy’s exclusion for claims arising out of the policyholder’s “own work,” a major benefit to construction contractor policyholders).

⁸⁵ “Business risk” exclusions refer to a related group of exclusions found in the standard form CGL policy that are designed to prevent the policyholder from receiving general liability insurance coverage where the plaintiff’s claim alleges mere failure of the policyholder’s work or product to satisfy the plaintiff customer or otherwise comply with contract specifications. Such cases of business dissatisfaction between a vendor policyholder and a customer complainant are considered business risks that should be borne by the policyholder in a de facto self-insurance of sorts. See *STEMPEL ON INSURANCE CONTRACTS*, *supra* note 3, at § 14.13 (also discussing “your property,” “impaired property,” contractual liability, and other business risk exclusions).

In this coverage battle, policyholders (typically contractors involved in the building of the homes at issue) had a major ally in the “subcontractor exception” to the “your work” exclusion. As the name implies, the subcontractor exception states that an otherwise applicable exclusion barring coverage for claims arising out of the defendant’s work is not applicable if the work was performed through a subcontractor.⁸⁶ Because this is the norm in modern home construction, the subcontractor exception effectively negated the “your work” exclusion for policyholder defendants who were general contractors or higher-level subcontractors (e.g., the subcontractor who used a sub-subcontractor to do the actual work). The subcontractor exception was one of the few coverage-broadening aspects of the 1986 revisions to the CGL policy. It was adopted at the request of the building community and agreed to by CGL insurers because it made the CGL more attractive to builders facing claims and facing the “your work” exclusion.⁸⁷ In short, it broadened coverage but was still acceptable or even attractive to insurers because builders would continue to buy the CGL policy and pay escalating premiums for the coverage because it saved them from shopping around for targeted construction defect coverage or self-insuring.

Since 1986, construction defect litigation boomed with a fury, even outpacing asbestos or pollution litigation in states that were more residential than industrial, such as Nevada and Arizona. Despite this, there appears to have never been a

⁸⁶ The “your work” exclusion removes coverage to the extent that the damage of which a plaintiff complains (when suing a builder) is to work done by the builder (i.e., the builder’s own product, such as a roof, a wall, or in the case of general contractors, potentially the entire home). The subcontractor exception restores coverage to the builder if the defective work of the builder-defendant was performed on its behalf “by a subcontractor,” which is frequently the case in modern construction. See ISO, CGL Form No. CG 00 01 12 07 (2006), reprinted in JEFFREY W. STEMPEL, ET AL., *PRINCIPLES OF INSURANCE LAW* 1289 (4th ed. 2011) (Appendix E). However, even without an exception, the “your work” exclusion does not bar coverage where the builder defendant’s defective work causes injury to another part of the home or building. For example, if a defective roof built by the policyholder allows water intrusion that damages the walls and floor built by others, coverage exists.

⁸⁷ See *O’Shaughnessy*, 543 N.W.2d at 99 (providing background on subcontractor exception to the “your work” exclusion). See also *supra* note 84.

serious attempt by insurers to eliminate the subcontractor exception. Although there have been some adjustments to CGL coverage prompted by construction defect litigation,⁸⁸ insurers continue to offer the product to builders notwithstanding their frequent claim in coverage litigation that the CGL is “not a performance bond.”⁸⁹ This reflects the continued strength of the inclusive model of general liability coverage.

Despite the contractions of the CGL form, most notably with the 1986 revisions, we largely continue, at least regarding general liability, to live in Elmer Sawyer’s world, albeit one that

⁸⁸ The “*Montrose* exclusion” or “*Montrose* endorsement,” which is really more of a batching clause, is named for *Montrose Chem. Corp. v. Admiral Ins. Co.*, 913 P.2d 878 (Cal. 1995), which in essence adopted a continuous actual injury trigger of coverage for consecutive liability insurance policies where the defendant policyholder was accused of causing property damage to the plaintiff. *Montrose Chem. Corp.*, 913 P.2d at 904. As long as some injury to property took place during each policy period, each policy was triggered. In the wake of the decision, insurers issuing general liability policies to construction contractors began including the provision, which states that where there is such continuing injury, all injury shall be deemed to have taken place during the policy period in which the continuously occurring injury first took place. This in turn has the effect of negating the continuous trigger that would otherwise apply by default rule of law and makes only one insurance policy responsible for the policyholder’s continuing infliction of this type of injury. See MALECKI & FLITNER, *supra* note 57, at 116–18.

⁸⁹ See, e.g., *Capstone Bldg. Corp. v. Am. Motorists Ins. Co.*, 67 A.3d 961, 984 n.31 (Conn. 2013) (insurer makes argument but is not successful); *Emp’rs Mut. Cas. Co. v. Donnelly*, 300 P.3d 31, 35–36 (Idaho 2013) (insurer successfully makes argument); *Kvarner Metals v. Commercial Union Ins. Co.*, 908 A.2d, 888, 892 (Pa. 2006) (same); *Nationwide Mut. Ins. Corp. v. Wenger*, 278 S.E.2d 874, 877 (Va. 1981) (same). The phrase, which is a staple of most all insurer briefs when defending a coverage denial of a construction defect claim, argues that if the policyholder’s defective work is remedied by the general liability insurer through paying a third-party claim, the CGL insurer has effectively been converted into a surety. Unlike a surety, however, the CGL carrier has no right to seek indemnification against the obligee whose poor construction required the surety to complete the construction or pay for it to be completed.

What this rallying cry of the CGL insurer in denial fails to acknowledge, however, is that in many construction defect cases the claimant is not alleging simply that the work was substandard or unsatisfactory and is not seeking merely to have it redone. In many cases, the construction defect has caused injury to other property. In such situations, the CGL insurer is not being asked to bond the defective work of the policyholder but rather is being asked to compensate the claimant when other property is damaged by the policyholder’s activity, a classic form of general liability.

narrowed during the latter twentieth century. The success of the CGL suggests resisting attempts to constrict the coverage. It also suggests the need to resist further fragmentation of the risk in other lines of insurance and to begin to move to a more inclusive model of coverage for these other insurance products. Moving to broader coverage throughout the product lines of the insurance industry holds substantial promise for all concerned constituencies.

III. THE RISK BUNDLING OF THE EARLY TO MID-TWENTIETH CENTURY IN OTHER INSURANCE PRODUCTS AND ITS APPARENT SUCCESS

I dwell a bit on Elmer Sawyer and the CGL story both because it is one I know better than the history of other lines of insurance and because it has received considerable attention in coverage litigation as policyholders typically invoke the history as a factor favoring broad construction⁹⁰ while some insurers resisting claims argue that the CGL should not be viewed as a pure “all risk” policy⁹¹ or a “performance bond,”⁹² and seek to

⁹⁰ Despite having seen Sawyer invoked by many policyholders’ briefs during the past twenty years—and often addressed by insurers seeking to refute any implication that Sawyer’s broad approach requires coverage in the instant matter), Sawyer remains seldom cited in treatises or cases. His work on the CGL form is prominent in STEMPER ON INSURANCE CONTRACTS, *supra* note 3, § 14.01 and in ANDERSON, ET AL., *supra* note 3, at §1.01, and is cited in U.S. Fire Ins. Co. v. J.S.U.B., Inc., 979 So. 2d 871, 893 (Fla. 2007) (holding that CGL coverage is available in construction defect claim) his CGL work is otherwise largely overlooked (his treatise on automobile insurance is cited in three cases). By comparison, Greg LeMond remains in relatively prominent public view.

⁹¹ See, e.g., George Tinker, *Comprehensive General Liability Insurance – Perspective and Overview*, 25 FED’N INS. COUN. QTRLY 215, 220 (1975) (“The history of the CGL is significant to an understanding of the policy. The name of the policy itself gains in meaning when viewed in its historic context. The CGL is ‘general’ only in contradistinction to ‘automobile.’ It is ‘comprehensive’ only in the sense that it combines certain historic forms of coverage into an integrated whole, with coverage being broadly stated in a single insuring agreement and exclusions circumscribing the limitations of the broad grant. The CGL is not, and was never conceived to be, an ‘all-risk’ liability policy.”). Tinker, Associate General Counsel for Kemper Insurance Companies at the time the article was written, overstates the case. While the CGL policy is not designed to be a multi-line policy, its structure is largely that of an all-risk policy

avoid coverage for somewhat out-of-the-mainstream actions such as negligent misrepresentation,⁹³ breach of lease,⁹⁴ chemically-connected injury that may or may not succumb to the pollution exclusion,⁹⁵ and construction defect claims.⁹⁶

for the type of risks addressed. *See* JERRY & RICHMOND, *supra* note 18 (suggesting that general liability coverage is in essence written on a all-risk basis, albeit typically with a rather significant list of standard exclusions). Tinker cites as his primary historical authority SAWYER, *supra* note 2. Tinker's reading of Sawyer is excessively grudging.

⁹² *See supra* note 89, discussing the “not a performance bond” defense to CGL claims.

⁹³ *See, e.g.*, *Sheets v. Brethren Mut. Ins. Co.*, 679 A.2d 540, 551 (Md. 1996) (finding claim of negligent misrepresentation in connection with home sale to fall within scope of CGL coverage).

⁹⁴ *See, e.g.*, *Vandenberg v. Superior Court*, 982 P.2d 229, 243 (Cal. 1999) (argument that breach of lease outside scope of CGL ineffective when alleged breach of lease by policyholder involved pollution that caused physical injury to tangible property and met policy definition of “property damage.” The court rejected the argument that CGL insurance covers only tort claims and not claims sounding in contract, focusing instead on whether, regardless of the legal classification of the claim, it involves alleged bodily injury or property damage); *Kazi v. State Farm Fire & Cas. Co.*, 15 P.3d 223, 233–34 (Cal. 2001) (finding no coverage under CGL policy for claim alleging breach of easement where court found no physical injury to tangible property from easement violation).

⁹⁵ *See, e.g.*, *Bituminous Cas. Corp. v. Sand Livestock Sys., Inc.*, 728 N.W.2d 216, 222 (Iowa 2007) (pollution exclusion construed to bar coverage for worker's death at hog confinement facility due to carbon monoxide poisoning from propane heater); *Am. States Ins. Co. v. Koloms*, 687 N.E.2d 72 (Ill. 1997) (rejecting insurer argument that pollution exclusion bars coverage for claim of carbon monoxide poisoning against policyholder policyholder stemming from faulty maintenance of furnace; *Cont'l Cas. Co. v. Rapid-American Corp.*, 609 N.E.2d 506, 513 (N.Y. 1993) (rejecting insurer attempt to apply a generalized pollution exclusion to asbestos claim injury); *see also* Jeffrey W. Stempel, *Reason and Pollution: Correctly Construing the “Absolute” Exclusion in Context and in Accord with its Purpose and Party Expectations*, 34 TORT & INS. L.J. 1 (1998). The question of the apt limits of the pollution exclusion can produce opinions that appear inconsistent even within the same state and court. *Compare* *Kent Farms, Inc. v. Zurich Ins. Co.*, 998 P.2d 292, 295 (Wash. 2000) (rejecting application of pollution exclusion to claim involving value failure that exposed worker refilling gasoline tank exposed to gasoline spurting from the tank, which caused immediate injury), *with* *Quadrant Corp. v. American States Ins. Co.*, 110 P.3d 733, 735 (Wash. 2005) (finding pollution exclusion applicable to claim by apartment building tenant of injury from fumes emanating from sealant used in treating deck). *See generally* RANDY MANILOFF & JEFFREY

But the story appears to be the same regarding other lines of coverage and other insurance products. After beginning as relatively targeted products, insurance policies evolved during the early-mid twentieth century into more comprehensive covers, most likely for the same reasons that animated the shift from individual liability policies to the CGL.⁹⁷ Then, as discussed further below, the late twentieth and early twenty-first centuries saw a move toward more curtailed coverage as insurers sought to limit exposure and isolate certain risks to a greater degree.⁹⁸

STEMPEL, GENERAL LIABILITY INSURANCE: KEY ISSUES IN EVERY STATE 323–380 (2d ed. 2012).

⁹⁶ See, e.g., *Am. Family Mut. Ins. Co. v. Am. Girl, Inc.*, 673 N.W.2d 65, 92 (Wis. 2004) (court rejects in insurer invocation of various defenses to coverage of construction defect claims against policyholder based on purported intentionality of activity and business risk exclusions where poorly done work caused injury to other property); *O'Shaughessy v. Smuckler Corp.*, 543 N.W.2d 99, 104–05 (Minn. Ct. App. 1996) (rejecting insurer interposition of “your work” exclusion in CGL to claim brought against an architect and general contractor due to the subcontractor exception that was part of the policy’s exclusion and was part of the standard CGL language due to construction industry preference and insurance industry interest in serving customer market). *But see* *Weedo v. Stone-E-Brick, Inc.*, 405 A.2d 788, 791 (N.J. 1979) (court accepts insurer argument that mere customer dissatisfaction with appearance of construction work is not a covered occurrence under standard CGL form). See generally MANILOFF & STEMPEL, note 95, Ch. 11.

⁹⁷ See generally SAWYER, *supra* note 2; Tinker, *supra* note 91. In similar fashion, automobile, homeowners’, and business property policies also expanded in basic scope during the mid-twentieth century. See, e.g., Weston, *supra* note 9 (describing generally the expansion of basic homeowners’ insurance during twentieth century).

⁹⁸ See Schwarcz, *Reevaluating Standardized Insurance Policies*, *supra* note 10 (finding substantial movement away from uniformly standard comprehensive coverage for homeowners’ policies and substantial overall constriction in coverage).

[A]s was the case with CGL policies, the coverage by “all risk” [property] policies has eroded over the years as insurers learned that certain risks or policyholders were not as profitable as the profit imperative demanded [citing examples of exclusionary language concerning earth movement, flood, certain windstorm damage, cyber loss, and mold].

* * *

[I]n addition, . . . ISO’s standard form “all risk” homeowners policy also contains exclusions for losses caused by (1) collapse; (2) frozen pipes; (3) wear

Automobile coverage provides a good example of both bundled coverage and a mid-century move toward broader coverage. For the most part, auto insurance is liability insurance in that its main goal is to protect policyholders from lawsuits and to protect their victims from impecunious tortfeasors.⁹⁹ All states require drivers to have auto insurance (or to demonstrate in some other fashion that they are sufficiently financially responsible to drive a potentially deadly two tons of steel capable of speeds in excess of 100 m.p.h.).¹⁰⁰ But the requirement is primarily that vehicle owners have liability insurance—albeit at woefully small amounts—with regulators relatively indifferent to the existence of other coverages. But most “no fault” states and some others require that the basic auto policy provide at least a modicum of first-party medical benefits and compensation for lost work, necessary domestic services, and the like.¹⁰¹ In addition, the typical auto policy also provides first-party property coverage on the vehicle for collision-related injury and damages from vandalism or the elements, which is styled as “comprehensive” coverage.

and tear; (4) mechanical breakdown; (5) corrosion or dry rot; (6) settling; (7) birds, vermin, rodents or insects; (8) ordinance or law; (9) power failure; (10) neglect; (11) war; (12) nuclear hazard; (13) intentional loss; and (14) governmental action. In short, as is the case under CGL policies, the profit imperative has reshaped the “all risk” property policy sold by insurers to homeowners today so that such policies cover quite a bit less than “all” risks.

French, *Profits Over Purpose*, *supra* note 9, at 24, 30.

⁹⁹ See generally DAVID D. THAMANN, BUSINESS AUTO: COMMERCIAL LINES COVERAGE GUIDE (2d ed. 2004); DAVID D. THAMANN, BUSINESS AUTO COVERAGE GUIDE: INTERPRETATION AND ANALYSIS (1998); DAVID D. THAMANN & MICHAEL K. MCCracken, PERSONAL AUTO COVERAGE GUIDE: INTERPRETATION AND ANALYSIS (1999); see also DORFMAN & CATHER, *supra* note 16, at 177–78; REJDA, *supra* note 18, at 205 (“Liability coverage (Part A) is the most important part” of the basic auto policy).

¹⁰⁰ See STEMPEL ET AL., *supra* note 16, at 987 (all states have financial responsibility laws that require automobile drivers to post security or have proof of liability insurance in order to obtain license plates and drive owned vehicles).

¹⁰¹ See *id.* at 897, 1041–43; ERIC A. WIENING & DAVID D. THAMANN, PERSONAL AUTO: PERSONAL LINES COVERAGE GUIDE 131–39 (2d ed. 2005); JACOB A. STEIN, STEIN ON PERSONAL DAMAGES § 5:69 (3d ed. 2013).

To be sure, there are some limits on the scope of auto coverage, particularly when claims arise from something other than the collision of two moving vehicles that produces a negligence claim. An oft-litigated issue is whether injuries alleged arose out of the use of an automobile, with jurisdictions dividing when faced with claims such as a mishap when using the car as a beast of burden,¹⁰² or from injuries incurred while sleeping in the vehicle¹⁰³ or pulled over on the side of the road.¹⁰⁴ States also divide as to whether the standard policy covers a vehicle's loss in value after an accident, as well as the cost of repairing physical injury.¹⁰⁵ But for the most part, auto coverage is broad coverage beyond the minimum mandated by the states.

The comprehensive nature of the standard auto policy appears not to have hampered the insurance industry. To be sure, auto insurance is not the easiest line to underwrite. Many prominent carriers occasionally have loss ratios or combined ratios in excess of 100. But some—such as, GEICO, USAA, and Progressive—regularly have either or both ratios below 100, which in essence means they are regularly profitable in spite of offering bundled coverage.¹⁰⁶ For the industry as a whole, the

¹⁰² See, e.g., *Cawthon v. State Farm Fire & Cas. Co.*, 965 F. Supp. 1262, 1269 (W.D. Mo. 1997) (vehicle used to attempt to remove tree stump, which had tragic results for child bystander when hit by flying stump upon its removal from the ground; no coverage).

¹⁰³ See, e.g., *MacKenzie v. Auto Club Ins. Ass'n*, 580 N.W.2d 424, 429 (Mich. 1998) (injuries from inhaling carbon monoxide when vehicle's engine used to provide warmth to adjacent camper attachment; no coverage).

¹⁰⁴ See, e.g., *Blish v. Atlanta Cas. Co.*, 736 So. 2d 1151, 1155 (Fla. 1999) (driver mugged by hooligans when changing flat tire on car; coverage).

¹⁰⁵ Compare *State Farm Mut. Auto. Ins. Co. v. Mabry*, 556 S.E.2d 114 (Ga. 2001) (auto insurer must compensate policyholder for the "inherent diminished value" loss of value of vehicle that has been in a collision even if fully repaired physically), and *Campbell v. Calvert Fire Ins. Co.*, 109 S.E.2d 572 (S.C. 1959) (same), with *Given v. Commerce Ins. Co.*, 796 N.E.2d 1275, 1277 (Mass. 2003) (rejecting inherent diminished value argument), and *Siegle v. Progressive Consumers Ins. Co.*, 788 So. 2d 355, 357 (Fla. 2001) (rejecting inherent diminished value).

¹⁰⁶ An insurer's loss ratio is the ratio of loss expenses relative to premium dollars collected. The insurer with a loss ratio below 100 is taking more in through premium receipts than it is paying in claims and is making an underwriting profit. The combined ratio is the amount of claims payments

combined ratio for the past decade has been roughly 100 or a bit lower.¹⁰⁷

Although one might feel sorry for the auto insurers with higher loss and combined ratios, they seldom go out of business – or even lose money – because of the time lag between premium collection and claims payment. There is a significant delay between the time of premium collection and the time of payment regarding the liability coverage component of the auto policy, which is not only the most important part of the policy's coverage, but also the element of coverage posing most risk exposure for the insurer. During the time between premium payment and any collisions and payments, the insurer invests the premium dollars. The resulting investment income goes to the insurer and is usually sufficiently large that even auto insurers with combined ratios significantly in excess of 100 can make money. Insurers with better loss ratios make even more money.¹⁰⁸ The same relationship exists for all types of liability insurers, some of which have much better loss ratios and longer intervals between premium collection and claims payment, which boosts investment income and allows the insurer to pay the claims in dollars that are less valuable due to intervening inflation.¹⁰⁹

Although generally liability insurers may gain the most from the time lag between premium collection and ultimate claims payment, all liability insurers enjoy this advantage. And

combined with administrative expenses relative to premiums collected. A company with a combined ratio below 100 is making an underwriting and overall operating profit.

¹⁰⁷ See INSURANCE FACTS AND STATS, *supra* note 16, at 14. This typical combined ratio and narrow range of variance applies not only to auto insurance as a whole, but also holds when private passenger and commercial auto insurance is separately examined. *Id.*

¹⁰⁸ See *supra* TAN and notes 39 and 62 regarding the role of “float,” which means using premium dollars until necessary for claims payment, and investment income in the insurer business model.

¹⁰⁹ See Stempel, *Assessing the Coverage Carnage*, *supra* note 27, at 351, 424, 432–33, 468 (liability insurers earn part of their profit by paying claims in dollars diminished in value by inflation compared to value of money at the time policies were sold years earlier).

although auto liability insurers may face claims sooner because injuries are more obviously immediate than with chemical, pharmaceutical, or construction defect injuries, the costs of defending the typical auto claim are likely to be lower than those required for the often more complex general liability. Director and officer, errors and omissions, and professional liability claims, if written on an occurrence basis, would likely fall in the middle of the continuum. But the standard practice of writing these risks on a claims-made basis both shortens the time between insured event and payment and reduces the carrier's exposure, particularly to long-tail claims. The net result benefits the insurer, who would otherwise write the risk on an occurrence basis.

In short, liability insurers, even those with most of their exposure in the litigious and plaintiff-friendly United States, can do pretty well, even though they may experience combined ratios above 100 with some frequency.¹¹⁰ By contrast, property insurers present a more sympathetic portrait, even if their combined ratios are often lower than those of liability carriers.¹¹¹ Unlike liability insurers, property insurers usually have substantially less time between receipt of premiums and payment of claims, depriving them of some of the opportunity to profit from investment or inflation.¹¹²

In addition, property insurers can be subjected to a large and immediate set of connected claims in a more dramatic fashion

¹¹⁰ See INSURANCE FACTS AND STATS, *supra* note 16, at 15.

¹¹¹ See *id.* at 16–23 (property or multi-peril insurers experience combined ratios above 100 with some frequency, but also often have ratios below 100, particularly for some narrower property coverages, such as crop insurance, inland marine insurance, surety, fire, and earthquake coverages).

¹¹² Property insurance is first-party insurance, which requires that when a valid claim is presented, the insurer must pay within a reasonable time. Although property claims disputes can drag on and even result in coverage litigation between policyholders and insurers, liability insurance generally entails more time between the insurer's receipt of premiums and the subsequent payment-requiring events of an injury to a third party, a claim, and a judgment against the policyholder. See generally M. Elizabeth Medaglia et al., *The "Concurrent Cause" Theory: Inapplicable to Environmental Liability Coverage Disputes*, 30 TORT & INS. L.J. 823 (1995) (comparing first-party and third-party insurance coverage).

than normally takes place for liability insurers, even those exposed to mass tort claims. Consider the example of a hurricane. Even if the insurer has worked hard to avoid highly correlated risk—e.g., insuring only beach front homes throughout the relevant season—a storm such as Sandy or Katrina can cause widespread injury to the insurer's pooled risk, and does so in one largely compressed time frame.¹¹³ By contrast, even large-scale torts take longer to erupt and are more dispersed in time and space. And rather than defending claims against the policyholder as does a liability insurer, property insurers are called upon to pay first-party claims within hours or days of the loss. The result is considerably more cash flow and financial pressure on property insurers even though (as noted above) disasters often provide the insurer with the opportunity to capture premiums that the public is willing to pay after having the dangers to its property highlighted by a catastrophe.¹¹⁴

Despite these pressures, property insurers generally moved toward more consolidated coverage during the mid-twentieth century. Homeowners insurance in particular became broader and more bundled in scope. Although there are several different

¹¹³ This is not to say that large destructive storms do not put a strain on the capital of even a well-run insurer with a large pool of uncorrelated risk. See Chad Hemenway & Mark E. Ruquet, *AIG Projects \$2B Sandy Loss; Chubb, Hartford, Hanover Among Carriers with Estimated Hundreds of Millions in Losses*, NAT'L UNDERWRITER, Dec. 13, 2012, at 6 ("Catastrophe modelers say Sandy could cause up to \$25 billion in losses for the insurance industry—placing it among the costliest disasters in U.S. history."); Ulrike Dauer, *Sandy's Insurance Bill Estimated at \$25 Billion for Industry*, WALL ST. J., Jan. 3, 2013, <http://online.wsj.com/article/SB10001424127887323374504578219293555274084.html> (estimating Sandy's losses for the insurance industry at \$25 billion and Katrina's losses at \$62 billion).

¹¹⁴ See generally PAYING THE PRICE: THE STATUS & ROLE OF INSURANCE AGAINST NATURAL DISASTERS IN THE UNITED STATES (Howard Kunreuther & Richard J. Roth eds., 1998) (tendency to purchase insurance after large loss rather than before noted throughout book). Although this tendency, a logical extension of the availability heuristic where people perceive more risk than is actually present from an event—e.g., shark bite, lightning strike, terrorist attack—that has been in the news, is almost intuitive regarding property insurance, it appears that life insurance purchases also increase in the wake of a natural disaster. See Stephen G. Fier & James M. Carson, *Catastrophes and the Demand for Life Insurance* (Manuscript July 9, 2009) (on file with author).

standard forms of homeowners insurance used, the most popular during the late-twentieth century was the HO-3 form,¹¹⁵ which provided comprehensive coverage, albeit through a list of covered perils on personal property rather than an all-risk insuring agreement, as was the case with the product's coverage on the dwelling. In addition, the insurer indemnified covered losses on the basis of the replacement cost of damaged home or personal property in the home.¹¹⁶ Like the CGL policy, the HO-3 proved popular with policyholders and a moneymaker for the insurers, as did the similarly comprehensive HO-2¹¹⁷ demonstrating that bundled coverage can be profitably written.

As with CGL insurance, insurers in these other lines of comprehensive coverage appeared to have done well financially offering this bundled coverage. Although insurers are quick to point out that they are at significant risk from information asymmetry, adverse selection, and moral hazard in underwriting liability risks, insurers are able to control these risks through effective design of liability policies in order to limit their exposure.¹¹⁸ Except in the softest of insurance markets, insurers

¹¹⁵ See Weston, *supra* note 9; French, *Profits Over Purpose*, *supra* note 9; see also DIANE W. RICHARDSON, HOMEOWNERS COVERAGE GUIDE: INTERPRETATION AND ANALYSIS (2d ed. 2002); Schwarcz, *supra* note 10, at 1273 ("In the homeowners insurance arena, the most commonly used form for stand-alone homes (rather than condominiums or mobile homes) is the 'HO3' policy.").

¹¹⁶ See Schwarcz, *Reevaluating Standardized Policies*, *supra* note 10, at 1273 ("The distinguishing features of this policy are that it provides 'all-risk' coverage for one's home and other structures (known as Coverages A and B in the ISO policy) but "named peril" coverage for personal property (known as Coverage C in the ISO policy). All-risk coverage protects property against all perils except for those that are explicitly excluded, whereas named-peril coverage protects property only against specifically enumerated perils.").

¹¹⁷ See Schwarcz, *Reevaluating Standardized Policies*, *supra* note 10, at 1273-74.

¹¹⁸ For a discussion of these basic insurance concepts, see JEFFREY W. STEMPEL, INTERPRETATION OF INSURANCE CONTRACTS 28-31 (1994); STEMPEL ET AL., *supra* note 16, Ch. 1; EMERIC FISCHER, PETER NASH SWISHER & JEFFREY W. STEMPEL, PRINCIPLES OF INSURANCE LAW Ch. 1 (3d ed. 2004). Regarding insurer capacity to respond to adverse events, "research has identified five main tools that almost all insurers use to one degree or another: risk-based pricing, underwriting, insurance contract design, claims management, and, less frequently, loss prevention services. In addition, some insurers and their trade

generally can draft policies to their liking, and of course, refuse to issue policies absent sufficient comfort with the risk and receipt of an adequate premium.¹¹⁹

Most important, both liability insurers and other carriers are the classic “repeat players” of the dispute resolution game.¹²⁰ If an insurer loses on a particular coverage point, it normally remains free to continue to litigate in other forums. Because insurers, like banks, normally are large repositories of capital, they are in a favorable position to win wars of attrition with both third-party claimants and policyholders simply by wearing them

associations also engage in research and education and, sometimes, even promote public safety regulation.” Tom Baker & Rick Swedloff, *Regulation by Liability Insurance: From Auto to Lawyers Professional Liability*, 60 UCLA L. REV. 1412, 1418 (2013). This is a rather powerful array of tools, particularly for companies that, if well managed, should be able to engage in long-term, disciplined planning through a diversified pool of risks and portfolio of investments. *But see id.* (finding regulation via liability insurance not as pervasively effective in practice as predicted by theory); Tom Baker & Sean J. Griffith, *The Missing Monitor in Corporate Governance: The Directors’ and Officers’ Liability Insurer*, 95 GEO. L.J. 1795, 1804 (2007) (finding similar results when examining impact of D & O insurance on corporate behavior).

¹¹⁹ A “soft” insurance market is one in which coverage is widely available at low prices as insurers compete aggressively to capture business and premium dollars. Conversely, a “hard” market is one in which conditions are not favorable for policyholders and coverage is restricted or available only at relatively high premium prices. *See* MARK S. DORFMAN, INTRODUCTION TO RISK MANAGEMENT AND INSURANCE 332 (8th ed. 2005) (“When insurance premiums increase significantly and some types of coverage become unavailable . . . [a] risk manager faces what they call a **hard market**. The opposite portion of the underwriting cycle, when insurance costs decline or insurers loosen underwriting standards, they call, logically enough, a **soft market**. As a rule of thumb, if insurance premiums equal or exceed 20 percent of the policy limit, the market is hard.”) (boldface in original).

¹²⁰ A repeat player is one that frequently participates in the dispute resolution system, while a “one shot” player is one that only occasionally engages in litigation or alternative dispute resolution. The repeat player has significant advantages in battling one shot players, including economies of scale, acquired expertise, institutional memory, familiarity with adjudicators, knowledge of forums, and the ability to spread losses and take the long view of a dispute. *See* Marc Galanter, *Why the “Haves” Come Out Ahead: Speculations on the Limits of Legal Change*, 9 L. & SOC. REV. 95, 98–100 (1974). Individual losses normally tend to be of relatively little consequence to the repeat player while they are often devastating to the one shot player. *Id.*

down to accept sub-optimal settlements—all the while continuing to earn investment income.¹²¹

But because of the pro-policyholder framework for assessing insurance coverage erected to counteract the inherent advantages held by insurers, insurers may find themselves with massive coverage obligations under certain circumstances. To take an obvious example, after a destructive hurricane, a windstorm insurer such as Citizens—Florida’s hurricane insurer of last resort—will be paying a lot of claims, and probably losing money in at least the short term, no matter how well it may have priced coverage or constructed the policy to avoid being required to also provide coverage for flooding or other destructive forces.¹²² But after large losses come large premium increases,¹²³ and for many working class and middle class Americans, forgoing hurricane insurance is now not likely to be seen as an option after the disastrous hurricane seasons of

¹²¹ See *supra* notes 39–44 (noting degree to which insurers earn substantial investment income on premiums with premium receipts predating payment requirements by years or even decades); *Assessing the Coverage Carnage*, *supra* note 27, at 362–63 (citing V.J. Dowling, Remarks at the University of Connecticut School of Law Insurance Law Center Symposium: Asbestos: Anatomy of a Mass Tort (Nov. 3, 2005)) (same).

¹²² See Liam Plevin, *Who Should Pay? As Number of Customers Rises For Insurers of Last Resort, Rates May Be Headed Up, Too*, WALL ST. J., Feb. 1, 2006, at B1, available at <http://online.wsj.com/news/articles/SB113876069708061726> (last visited Nov. 21, 2013) (noting Citizens’ losses after bad hurricane years of 2004 and 2005, but also noting that many Florida homeowners are “in no position to shop around” because the “only company offering a policy is Citizens Property Insurance Corp., Florida’s insurer-of-last-resort.”).

¹²³ See Susanne Sclafane, *Florida Homeowners Rates Could Triple, Citizens Warns*, NAT’L UNDERWRITER PROP. & CAS., Dec. 5, 2005, at 21, available at <http://www.propertycasualty360.com/2005/12/05/florida-homeowners-rates-could-triple-citizens-war> (last visited Nov. 2, 2013) (“We’re looking at a statewide average increase . . . of 60 percent, with many coastal areas receiving triple digit increases,” according to Robert Riker, president and executive director of Citizens Property Insurance Corp. in Florida—the state’s largest insurer of last resort.”). Although general liability insurance rate increases have been more gradual in response to the more gradual onset of asbestos mass tort insurance coverage, the same economic and marketing factors are at work. See George J. Church et al., *Sorry, Your Policy Is Canceled*, TIME, Mar. 24, 1986, at 16–18 (describing abrupt rises in select liability insurance premiums).

2004 and 2005. Consequently, insurers are in a relatively good position to recoup past losses through future price increases.

Even if this were not the case, there is nothing unfair about a legal regime structured to give policyholders the benefit of the doubt in close cases after the policyholder has established that a claim comes within coverage, or is potentially within coverage if the question centers on the duty to defend). An insurance policy is an aleatory contract, one in which the value of the exchange may be lopsided depending on the contingencies involved.¹²⁴ In similar fashion, liability insurers underwriting asbestos policyholders prior to the advent of the asbestos mass tort may have been in a favorable business position. From the time of the CGL policy's introduction in the 1940s until the arrival of asbestos and pollution claims in the 1970s, the CGL appears to have been a business success and large moneymaker for the insurance industry.¹²⁵ But when the asbestos mass tort arrived, the basic contractual and legal framework of coverage determination combined with the peculiarities of asbestos to require coverage beyond that anticipated by insurers when they first accepted the risk. This may have made the CGL less profitable, but it hardly brought the liability insurance industry to ruin.¹²⁶

¹²⁴ See *infra* TAN 263–270.

¹²⁵ See *supra* TAN 61–90.

¹²⁶ See *supra* TAN 61–90; see also *supra* note 58 (describing asbestos loss amounts); see Fitch Ratings, *Special Report, Asbestos: Impact on U.S. Insurance Industry*, July 25, 2002 at 9 (“[U]ltimately, the development of asbestos claims will have a moderately negative impact on insurer ratings during the next few years.”) and at 1 (although asbestos liabilities will produce a “slow bleed” that will depress future earnings for many years” the “historic asbestos earnings drag has average 1.7 combined ratio points for the commercial lines/reinsurance sectors over the past few years” although near-term future losses may be more significant because of surge in second generation claims in late 1990s and early 21st Century); Lehman Brothers Global Equity Research, *Thinking About Asbestos*, March 20, 2002 at 27 (insurer earnings drag from asbestos can reasonably be estimated at 1.5 percent); Insurance Journal, *Fitch Affirms Rating for St. Paul Travelers Ratings After Asbestos Charge; Outlook is Stable*, Jan. 31, 2005, <http://www.insurancejournal.com/news/national/2005/01/31/50493.htm>. But see *Asbestos Liability Takes an Insurer Out*, RISKPROF (June 8, 2004, 3:26 PM), available at http://riskprof.typepad.com/tort/2004/06/asbestos_liabil.html.

IV. THE MOVE TOWARD FRAGMENTATION AND SWISS CHEESE COVERAGE

Despite the seeming profitability of bundled and broad insurance products, insurers appear to have moved away from it. As the Conference organizers have observed, there appears to be a trend toward fragmented coverage and fragmented coverage may be less useful to almost all affected contingencies than is broad-based comprehensive coverage.¹²⁷ The seeming move to less comprehensive coverage presents the cluster of problems previously noted: reduced policyholder knowledge and correspondingly less efficient markets; gaps in coverage and consequent ripple effects of inadequate protection and compensation; increased uncertainty and disputes, including wasteful litigation.¹²⁸

Examples of the new world of more fragmented coverage abound. Perhaps most prominently, homeowners insurance and other first-party property insurance typically excludes coverage for water damage and earth movement, as well as contamination.¹²⁹ If a small business or homeowner wants to be sufficiently protected from these risks, as well as those of fire, wind, theft, and vandalism, these separate coverages must be

¹²⁷ See Program Announcement for A Conference on Fragmented Risk, *supra* note 7 (Sometimes, perhaps increasingly . . . insurance policies fragment risk Fragmenting allows insurers to exclude coverage for correlated risks where potential losses are high and to reduce premium costs to respond to market conditions. Fragmenting also reduces potential liability for new and unanticipated risks, especially due to technological change or expansive judicial interpretation of policy language; what began with questions about coverage for pollution and asbestos has now spread to mold, Chinese drywall, and even climate change.)

¹²⁸ See Program Announcement for A Conference on Fragmented Risk, *supra* note 7.

¹²⁹ Standard homeowners' and commercial property policies include coverage for direct physical injury caused by windstorms, which of course includes large windstorms such as a hurricane. However, these same policies expressly exclude coverage for water damage unless the release or discharge of water springs from an event such as a burst pipe or overflowing dishwasher. Flood insurance is available through the same agents selling property insurance policies, but must be purchased via a separate policy sold pursuant to the federal flood insurance program.

purchased. This is not impossible. Many insurers offer an earth movement endorsement in return for an additional premium and imposition of a larger deductible in connection with such claims.¹³⁰ The federal government offers flood insurance at attractive rates because they are taxpayer subsidized.¹³¹ More difficult to obtain, at least at an attractive price, is environmental impairment insurance, but a determined prospective policyholder can usually obtain it.¹³² But purchasing insurance in this manner is not efficient and leaves many under-informed or insufficiently dogged policyholders with significant gaps in coverage.

In addition, some policy language, if enforced literally by courts in coverage disputes, seems but a trap for unwary policyholders. For example, many property insurers not only have an earth movement exclusion, but also an “anti-concurrent causation” clause. That clause provides that even if the loss was

¹³⁰ The standard personal or commercial property policy excludes coverage for “earth movement,” which of course excludes damage from earthquakes, with exceptions to the exclusion varying by policy type and insurer.

¹³¹ The National Flood Insurance Program, established in 1968 and subsequently modified, allows private insurers to sell federal flood insurance, collect the premium, and receive an expense allowance from the U.S. government for policies written and claims paid, with the government absorbing all underwriting losses. Property owners with federal guaranteed financing for their property must purchase this insurance if the property is located in a flood zone as determined by federal mapping of communities. See REJDA, *supra* note 18, at 262–63.

¹³² Although insurers have since 1986 largely excluded coverage for pollution-related losses, in most markets, Environmental Impairment Insurance is available for an additional premium. Typically, these policies are written on a claims-made basis, with coverage limited to relatively abrupt pollution discharges confined in time and space. The market for these products is normally relatively “hard,” meaning that large policy limits are not often available and premiums are relatively high. See APPLEMAN ON INSURANCE, §193.02[C] (describing specialized forms of environmental liability insurance) (Chapter 193, *Environmental Insurance*, by William G. Beck, et al., published in 2008 APPLEMAN volume); MARK S. DORFMAN, INTRODUCTION TO RISK MANAGEMENT AND INSURANCE 332, 381–86 (8th ed. 2005) (defining hard and soft insurance markets and describing insurer concern about providing broad pollution liability coverage and use of EIL policies as an alternative, noting that EIL policies use the more restrictive claims-made format less useful to policyholders).

caused in part by covered perils, as well as excluded earth movement, there is no coverage so long as earth movement was in any way involved in bringing about the loss.¹³³

A. THE INCREASINGLY INCONSISTENT AND POROUS HOMEOWNERS POLICY

A recent study of homeowner's insurance found substantial variance in the policy provisions, with most deviations from the standard ISO form restricting coverage, often in ways that would be at odds with the average policyholder's concept of basic homeowners insurance protection.¹³⁴ In addition to the frequent use of anti-concurrent causation clauses, homeowners insurers frequently reduced coverage through the following: increase of the hazard clauses;¹³⁵ mold exclusions;¹³⁶ water damage

¹³³ See also Schwarcz, *supra* note 10, at 1280–81 (finding substantial variance in available homeowners' insurance forms in several states, with a significant number limit coverage though literal application of a broad anti-concurrent causation clause); French, *Profits Over Purpose*, *supra* note 9, at 23–30 (describing limitations on seemingly broad homeowners and other property coverage in the standard forms themselves); see e.g., *Bentoria Holdings, Inc. v. Travelers Indem. Co.*, 980 N.E.2d 504 (N.Y. 2012) (enforcing exclusion precluding coverage for loss due to excavation activities, a type of earth movement that is far less widespread and threatening to risk pools and insurer profit than natural earthquakes or mudslides).

¹³⁴ See Schwarcz, *supra* note 10, at 1280–1317.

¹³⁵ See *id.* at 1282–85 (finding many insurers using such clauses in place of standard HO-3 language). An increase of the hazard or increase of the risk clause is one that negates otherwise available coverage if the policyholder has engaged in conduct that has increased the risk of loss or perhaps even if the policyholder has failed to protect property that has been endangered. As Professor Schwarcz observes, a clause of this type might strip the policyholder of coverage for failing to take action if a nearby tree is on the verge of collapse while an increase of risk clause could negate coverage because the policyholder improperly installed an air conditioner.

¹³⁶ See *id.* at 1285–86. Mold exclusions, which have become common in the wake of a rash of mold-related claims in the late 1990s and early 2000s, generally bar coverage for losses arising out of mold or fungus, unless it was hidden within walls, floors, ceilings, or was caused by either the accidental discharge or overflow of water.

exclusions or limits;¹³⁷ pollution exclusions;¹³⁸ restrictions on theft coverage;¹³⁹ restrictions on collapse coverage;¹⁴⁰ limits on electric current damage coverage;¹⁴¹ sublimits on coverage of certain property;¹⁴² avoiding coverage for ordinance or law

¹³⁷ See *id.* at 1293–94. As the name implies, water damage exclusions bar coverage for losses arising out of water damage, more specifically gradual water damage, with coverage generally being restored if there is an abrupt water release or discharge. Such exclusions were also a common substitution for standard HO-3 policy language.

¹³⁸ See *id.* at 1287. Pollution exclusions barring coverage for losses arising out of the release or discharge of a long list of pollutants, such as dust, dirt, any “chemical” were also common.

¹³⁹ See Schwarcz, *supra* note 10, at 1288. Theft was often not covered under homeowner policies unless there were “visible marks” of physical injury to the exterior of the covered building. *Id.* The intent of such exclusions is to avoid cover fraud losses that do not result from a burglary or where the burglary is an inside job. But such exclusions are probably not very effective at anything other than disappointing the reasonable expectations of the policyholder. An unscrupulous policyholder wishing to stage a burglary and collect for the feigned loss of inventory or other property need merely break a window or lock on the way out, presumably while wearing gloves so not to leave fingerprints. See *id.*

¹⁴⁰ See *id.* at 1289. Collapse is a peril historically covered by the homeowners’ policy. However, an increasing number of insurers are modifying the basic HO-3 form to exclude even a total collapse of the insured structure, unless it is brought about by a specifically enumerated peril. *Id.*

¹⁴¹ See *id.* at 1289–90. In what must be a surprise to the average homeowner policyholder, many policies now exclude coverage for damage stemming from artificial electric current. *Id.*

¹⁴² See *id.* at 1290–91. With increasing frequency, homeowners’ policies often have sublimits for coverage of property thought by insurers to present greater risk of loss or moral hazard than found for ordinary property and the dwelling itself. For example, there may be substantial reductions in coverage for damaged or stolen jewelry, electrical equipment, furs, china, or art, although the policyholder may through additional premium be able to raise these sublimits. Items such as these present insuring difficulty because they are both relatively high in value for their size and weight and can be readily moved. For example, a policyholder tempted to defraud an insurer can secret jewelry or furs and report a phony burglary, receive compensation, and then unpack the jewelry or furs from hiding. Fraud of this sort is much more difficult with regard to claims of loss involving large appliances, furniture, or fixtures. Consequently, insurers often seek through sublimits to reduce their risk exposure for items that more easily facilitate false claims.

related costs;¹⁴³ restrictions on policyholder recovery due to subrogation priority;¹⁴⁴ and limits on liability coverage for both bodily injury and property damage.¹⁴⁵ In addition, there are other restrictions on liability coverage such as limitations based on the nature of alleged injury,¹⁴⁶ a constricted definition of an “occurrence,”¹⁴⁷ an expanded expected-or-intended injury exclusion,¹⁴⁸ criminal acts exclusions,¹⁴⁹ or events involving alcohol or drug use.¹⁵⁰ Further, many homeowners policies do

¹⁴³ See *id.* at 1292–93. Where rebuilding insured property is made more expensive because of intervening changes in the laws or regulations affecting the property—such as a requirement of stronger glass, a raised foundation near water, etc.—many insurers now include provisions barring coverage for this increment of the loss. *Id.* These provisions have not typically been in the standard form policy.

¹⁴⁴ See *id.* 1294–95. Many insurers have been modifying the standard HO forms to give themselves increased subrogation priority and the right to be paid ahead of the policyholder if a recovery can be obtained from a third party that caused the loss to the insured property.

¹⁴⁵ See Schwarcz, *supra* note 10, at 1295–97. The standard homeowners’ policy has long also provided a modicum of general liability insurance for the policyholder that has been sued for injuries to a guest or business vendor (e.g., a dog bit, a slip on a slippery floor). Many insurers have modified this to limit the range of bodily injury covered by taking away coverage for mental injury claims or loss of use property damage claims. *Id.* at 1295–96.

¹⁴⁶ See *id.* at 1298. For example, some policies take away coverage for third party claims of injury resulting from intentional conduct by the policyholder even if the resulting injury was not intended. *Id.*

¹⁴⁷ See *id.* at 1297–98. Covered occurrences may take place in multiple policy periods. However, many insurers now exclude coverage if the occurrence began prior to its policy period. *Id.*

¹⁴⁸ See *id.* at 1298–99. Historically, there was a self-defense exclusion to the intentional injury exclusion found in most liability coverage. Increasingly, insurers are narrowing or eliminating the self-defense exception. *Id.* at 1299.

¹⁴⁹ See *id.* at 1299–1300. Injuries resulting from conduct deemed as criminal may be excluded even if the injury was not expected or intended from the standpoint of the policyholder. *Id.*

¹⁵⁰ See *id.* at 1301. For example, social host liability due to a guest’s consumption of alcoholic beverages on the insured premises is now often excluded. *Id.*

not provide coverage for personal injury liability claims¹⁵¹ or liability assumed by contract.¹⁵²

Homeowners insurance also appears to now provide more limited coverage than before because of the manner in which insurers may more aggressively deny coverage pursuant to the traditional business pursuits exclusion contained in such policies. The business pursuits exclusion, as the name implies, bars coverage for losses incurred as a result of business being conducted by the policyholder in the insured home.¹⁵³ This can include damage to the home due to commercial activities being conducted in the home (e.g., running a bakery out of the kitchen with an overheating oven starting a fire that damages the home) or liability claims lodged against the policyholder by a customer of a policyholder's business run out of a home (e.g., a patron of the bakery in the home slipping on melted butter in the hallway and incurring injury).

The overall rationale of the business pursuits exclusion is perfectly sensible. Commercial enterprises generally pose greater risks of property loss or third-party liability claims than do mere residences. The average homeowner's activity is less likely to lead to fire, explosion, or large theft losses than that of the average business involved in significant manufacturing, construction, or storage of a sizeable amount of valuable inventory or expensive machinery. The average homeowner

¹⁵¹ See Schwarcz, *supra* note 10, at 1303–04. In general liability parlance, “personal injury” is typically distinguished from bodily injury in that personal injury coverage usually extends to certain intentional torts such as trespass, defamation, and trademark infringement. *Id.* Insurers are increasingly removing this type of liability coverage from the standard homeowners’ policy. *Id.*

¹⁵² See *id.* at 1300–01. In many instances, standard form contracts shift liability risk to the party that must adhere to an adhesion contract. “Given the pervasiveness of these types of agreements, it is not surprising that the standard HO3 policy covers liability resulting from the assumption of another’s liability, so long as this occurs prior to the liability-generating occurrence. . . . [H]owever, this is not true of many of homeowners policies. . . .” issued by many insurers. *Id.* at 1300.

¹⁵³ See MARK S. DORFMAN, INTRODUCTION TO RISK MANAGEMENT AND INSURANCE 206–07 (8th ed. 2005). The standard homeowners’ policy excludes coverage for losses arising out of business pursuits of the homeowner conducted on the insurance premises.

living his or her life is less likely to injure another person than is the average business that may be dropping, bumping, despoiling, mis-installing, or manufacturing a defective product.

But the business pursuits exclusion can be carried too far if applied to only modestly remunerative activity, such as babysitting, conducted in an insured home. Historically, insurers appear not to have attempted to enforce the exclusion, and if they did courts were unlikely to support such efforts to deny coverage. But insurer and judicial attitudes may be drifting toward litigation conduct and results that are the functional equivalent of broader business risk exclusion.

Consider *Dwello v. American Reliance Insurance Co.*,¹⁵⁴ the homeowner provided regular babysitting for a neighbor, seemingly as an accommodation to the neighbor's work demands, and was paid (modestly but enough that it amounted to roughly forty percent of the policyholder's modest overall income).¹⁵⁵ While the neighbor's child was in the house, the homeowner's dog bit the child, causing significant injuries.¹⁵⁶ The neighbor sued the homeowner, who in turn sought coverage pursuant to the liability portion of her homeowner's policy.¹⁵⁷ The insurer denied coverage, invoking the business pursuits exclusion – and prevailed before the trial court and the Nevada Supreme Court¹⁵⁸ in a decision subject to criticism.¹⁵⁹

¹⁵⁴ *Dwello v. Am. Reliance Ins. Co.*, 990 P.2d 190 (1999).

¹⁵⁵ *Id.* at 191.

¹⁵⁶ *Id.*

¹⁵⁷ *Id.*

¹⁵⁸ *See id.* at 191–92.

¹⁵⁹ *See* Roger O. Steggerda, Note, *Watching Your Neighbor's Child: Is Babysitting Really a Business Pursuit? A Comment on Dwello v. American Reliance Insurance Company*, 1 NEV. L.J. 323, 336 (2001). In the same vein are court decisions denying coverage for what appear to be innocent policyholders due to criminal misuse of their property. *See* Gaynor Pengelly, *Sorry, Your Home's a Dope Farm so You're Not Insured: Cannabis Farmers Trashed my Cherished Buy-to-let*, DAILY MAIL (May 11, 2013), <http://www.dailymail.co.uk/money/mortgageshome/article-2323042/Sorry-homes-dope-farm-youre-insured.html> (landlord policyholder not covered for damage to property where tenants were growing marijuana on premises; describing general trend toward such strict enforcement of illegal activities or

As a literal manner, the homeowner was perhaps engaged in a commercial enterprise by receiving pay for a service, but this sort of limited, episodic, informal babysitting normally presents few risks of third party claims greater than what might arise from simple play dates at the insured home involving friends of the homeowner's child. Although insurers may be reluctant to dispense with the exclusion altogether, one might expect a relaxed attitude toward its invocation and enforcement. But in *Dwello*, the insurer treated the neighborly babysitting as the equivalent of the homeowner's operation of a gymnastics studio or large-scale nursery—and prevailed, notwithstanding the questionable persuasiveness of its argument.¹⁶⁰

Insurers also appear to be more aggressively denying coverage for homeowner liability claims involving criminal conduct by the policyholder, even in the absence of an express criminal acts exclusion in the policy. And despite the absence of such specific exclusions, courts have sided with the insurers on a disturbing number of occasions, invoking either an excessively expansive view of the “expected or intended” exclusion or notions of public policy.

*Minnesota Fire & Casualty Co. v. Greenfield*¹⁶¹ presents a disturbing example. Homeowner Greenfield dealt drugs,¹⁶²

criminal acts exclusions in insurance policies). Although the particular decision discussed was in England, a jurisdiction traditionally taking a more formalist and textualist view of contracts than most American states, it seems an undue forfeiture of purchased insurance, assuming the landlord really was unaware of the tenant activities.

¹⁶⁰ And insurers have been willing to litigate the exclusion in such small potatoes babysitting cases, with considerable success. *See, e.g.,* Am. Commerce Ins. Co. v. Few, No. 10-CV-0036-CVE-FHM, 2010 U.S. Dist. LEXIS 63037 (N.D. Okla. June 24, 2010); Concord Gen. Mut. Ins. Co. v. Thomas, No. 816-12-07, 2009 Vt. Super. LEXIS 79 (May 27, 2009) (applying business pursuits exclusion to bar coverage for family member's liability incurred during part-time job as bartender; noting that most courts find exclusion applicable if there is continuity of business activity and profit motive even where work in question is not primary occupation of insured).

¹⁶¹ 855 A.2d 854 (Pa. 2004).

¹⁶² Greenfield appears not to have been a full-time drug dealer. The opinion refers to him leaving in the morning “for work” in a context that suggests the work was something other than drug dealing. *Id.* at 857. The opinion also notes that Greenfield claimed to sell drugs, though “mostly just weed” only

including a heroin sale to customer Angela Smith, who ended up passing out at Greenfield's house for the night. Leaving the next morning, Greenfield instructed a still-alive Smith to lock the door if she left.¹⁶³ She was dead of a heroin overdose when Smith returned.¹⁶⁴ After an abortive attempt to conceal the death, Greenfield contacted the police anonymously to report the body, but was discovered by police and pled guilty to involuntary manslaughter.¹⁶⁵ Smith's understandably distraught parents brought a wrongful death action against Greenfield, who sought defense and coverage from his homeowners' insurer.¹⁶⁶ Minnesota Fire denied coverage, invoking the expected or intended injury defense and contending that Smith's death was not a sufficiently accidental offense to fall within coverage.¹⁶⁷ The trial court disagreed and held that the insurer was obligated to defend the claim.¹⁶⁸ Invoking public policy based on the illegality of the use or sale of heroin, as well as a doctrine of "inferred intent" (the notion that the court could discern an intent to inflict injury from the policyholder's reckless conduct), the Pennsylvania Superior Court reversed and denied coverage.¹⁶⁹ The Supreme Court of Pennsylvania rejected the inferred intent analysis but affirmed the result, also on public policy grounds, essentially holding that it would violate public policy for Greenfield to obtain insurance for liability arising out of criminal activity.¹⁷⁰

"occasionally," with heroin sales to only a select few customers. *See id.* at 856–57.

¹⁶³ *Id.* at 857.

¹⁶⁴ *Id.*

¹⁶⁵ *Id.* at 857.

¹⁶⁶ *Id.* at 858–59.

¹⁶⁷ *Id.* at 858–59.

¹⁶⁸ *Greenfield*, 855 A.2d at 859.

¹⁶⁹ *Id.* at 860.

¹⁷⁰ *Id.* at 865–68.

Greenfield is something of a judicially activist disaster.¹⁷¹ The court majority concedes that *Greenfield* did not have a subjective or specific intent to hurt Smith.¹⁷² Drug dealers tend to make more money off live customers than dead ones. The majority also conceded that the policy contained no exclusion for losses or liability arising out of drug use or other criminal activity.¹⁷³ Nonetheless, the majority gave the insurer the benefit of such an exclusion despite its absence in the policy, reasoning that because drug use is illegal, the Commonwealth of Pennsylvania surely would not want drug sellers to have the benefit of liability insurance if sued by customers (or their estates or parents).¹⁷⁴ Only two Justices dissented.¹⁷⁵

¹⁷¹ The opinion is also a pretty ham-handed rhetorical exercise in that it contains several gratuitous pieces of information or turns of a phrase designed to convince the reader of *Greenfield*'s essential sleaziness that presumably justifies stripping him of contract rights. For example, we are told that prior to Smith's arrival, "*Greenfield* had been drinking Mad Dog beer and was under the influence of marijuana and heroin." *Id.* at 856. *Greenfield*'s drinking of "Mad Dog" beer was presumably intended as more evil and dangerous than if he had been quaffing a Leinenkugel Summer Shandy or a Chimay Blue. But *Greenfield*'s taste in libations is an irrelevant but prejudicial fact.

Similarly, the majority notes that the bag of heroin sold to Smith was labeled "Suicide." *Id.* at 857. So, in many parts of the country, is the mixture of various soft drinks (usually cola, root beer, orange and lemon-lime with perhaps some Dr. Pepper) favored by pre-teens at junior high basketball games or county fairs. The majority also provides great detail about *Greenfield*'s attempt to essentially dump Smith's body away from his home in order to avoid detection. *Id.* As another Pennsylvanian, the late Third Circuit Judge Ruggerio Aldisert put it memorably: "Basta!" [Italian for "enough"]. See *United States v. Desmond*, 670 F.2d 414, 420 (3d Cir. 1982)(Aldisert, J., dissenting) (arguing that it is time for a bright line rule against special verdicts in criminal cases unless requested by defendant). We know that *Greenfield* is not the kind of guy you want your daughter to bring home (much less elope with), but none of that is germane to the coverage question at issue in the case.

¹⁷² *Greenfield*, 855 A.2d at 866–68.

¹⁷³ *Id.* 867–68.

¹⁷⁴ *Id.* at 872–73. Showing amazing callousness toward the victim, the Court majority observed that "Smith was a willing participant in a criminal transaction." *Id.* at 868. By this logic, any kid using marijuana would be denied recovery if injured by a drug dealer, "pot party" host, or other person involved in use of this commonly consumed but illegal substance.

Cases like *Greenfield* are also something of a public policy disaster. Although one struggles to find sympathy for the seemingly careless and callous Greenfield, there is no difficulty finding sympathy for Smith and her family, which of course is the group that suffers from the court's decision. Unless Greenfield was a Pennsylvanian Pablo Escobar, he probably lacked the personal assets to provide adequate compensation to his victims. Denying insurance to Greenfield only denied compensation --and some small measure of justice--to Smith and her family. Even in the absence of a textual defense to coverage, the promised comprehensive protection (and social utility) of the homeowner's policy may be fragmented by judicial error.

B. THE INSIDIOUSNESS OF THE "ANY INSURED" EXCLUSION

Denial of coverage to one insured due to the sins of another presents another area in which homeowner's coverage has narrowed, and that has implications for other policies as well.¹⁷⁶ Historically, most states appeared to apply an "innocent co-insured" doctrine under which a policyholder who was not involved in coverage-destroying conduct would at least collect a pro-rated share of policy proceeds after a loss.¹⁷⁷ A typical scenario involves one spouse engaged in criminal activity while the other is unaware or unable to stop it. Another common scenario is one of divorcing spouses in which one spouse breaks into, vandalizes, or otherwise injures a home in an expression of

¹⁷⁵ *Id.* at 872–73 (Cappy, J., joined by Nigro, J., dissenting) (accusing majority of rewriting the policy for the benefit of the insurer that drafted the policy and also noting concern "about the potential sweeping reach of the majority's decision," which suggested that insurers need not provide coverage for any damages arising out of conduct the legislature has defined as criminal).

¹⁷⁶ See generally MANILOFF & STEMPEL, *supra* note 95, Ch. 10.

¹⁷⁷ See, e.g., *Travelers Indem. Co. v. Bloomington Steel & Supply Co.*, 718 N.W.2d 888, 895 (Minn. 2006) (where insurer chooses to frame coverage exclusion in terms of conduct by "the" insured, court may conclude that only misconduct by the named policyholder defeats coverage); *Kulubis v. Tex. Farm Bureau Underwriters Ins. Co.*, 706 S.W.2d 953 (Tex. 1986). See generally Brent R. Lindahl, Comment, *Insurance Coverage for an Innocent Co-Insured Spouse*, 23 WM. MITCHELL L. REV. 433 (1997).

anger. A spouse or other co-insured (e.g., a business partner) who could demonstrate lack of fault could often recover at least a pro-rata share of available insurance proceeds. For example, if the husband destroyed the family home in a meth lab explosion, committed arson as part of insurance fraud, or burned the home in reaction to an impending end of the marriage, the courts allowed the innocent wife to receive half the insurance policy limits.¹⁷⁸

But the bulk of these older cases more charitable-to-blameless spouses and other innocent co-insureds contained language barring coverage if there was misconduct by “the insured.”¹⁷⁹ Most courts faced with this language found the term either intended to refer only to the named insured on the declarations sheet of the policy or sufficiently ambiguous that it must be construed in favor of the innocent co-insured.¹⁸⁰ In response, insurers replaced the “the insured” language with “an insured” or “any insured.”¹⁸¹ Since making these changes insurers have fared far better, prevailing in the bulk of coverage actions.¹⁸² Essentially, the innocent co-insured doctrine has been legislatively overruled via the private legislation of the insurance industry moving to more expansive exclusionary language that narrows and further fragments coverage.

A disturbing recent example is *Postell v. American Family Mutual Insurance Co.*¹⁸³ Faced with impending divorce, the husband returned to the couple’s home (from which he’d moved out), ignited it, and intentionally committed suicide in the blaze.¹⁸⁴ The wife sought to obtain coverage for the destruction

¹⁷⁸ See, e.g., *Kulubis*, 706 S.W.2d at 953.

¹⁷⁹ See MANILOFF & STEMPEL, *supra* note 95, Ch. 10.

¹⁸⁰ See *id.* at 226–27.

¹⁸¹ See *id.* at 227–29.

¹⁸² See MANILOFF & STEMPEL, *supra* note 95, Ch. 10; See, e.g., *Minkler v. Safeco Ins. Co.*, 232 P.3d 612, 623–24 (Cal. 2010).

¹⁸³ 823 N.W.2d 35 (Iowa 2012).

¹⁸⁴ The Court embraced this hard-core textualist and formalist position notwithstanding that it resulted in a complete denial of insurance protection negating the purpose of the policy and the expectations of the surviving wife,

of the home, which she had intended to occupy after the divorce was final and the husband moved out.¹⁸⁵ A unanimous Supreme Court of Iowa denied her claim and backed the insurer's position on the exclusion.¹⁸⁶

One can certainly criticize these cases in which the insurer obtains from courts a broad construction of an exclusion, or text that operates in the same nature as an exclusion, to reverse a long-standing doctrine effectively preventing excessive forfeiture of insurance benefits by innocent policyholders. But absent jurisprudence more favorable to those policyholders, the move from excluding coverage for misconduct by "the" insured to excluding coverage based on conduct by "any" insured is a significant step toward more restricted and fragmented coverage. This fragmentation appears in the ascendance for both homeowners and general liability coverage.

C. CURTAILMENT OF THE CGL POLICY

Even the CGL policy, my comparative paragon of bundled coverage, has slipped a bit since its glory days in the 1960s and

who surely could not imagine either that her husband could do such a thing or that, in doing so, he would destroy the insurance benefits they had purchased from years of premium payments. They had lived in the now destroyed home since 1989 and had been married for thirty years. *Id.* at 38. In addition, the husband, who despite having burns over eighty percent of his body, did not die for three days, was deemed mentally ill by the medical professionals treating him after the fire. *See* 823 N.W.2d at 38–39 (providing extensive discussion of events leading up to husband's immolation, destruction of the home, and medical treatment).

¹⁸⁵ *Id.* at 27, 39.

¹⁸⁶ *Id.* at 37, 48. In no portion of the opinion, however, did the Court consider whether depriving the non-arsonist wife of coverage, which effectively made her homeless absent another source of funds for living expenses, because of the deranged acts of the husband was consistent with the overall injuring agreement and the purpose of the intentional injury exclusion on which the insurer's defense was based. For a more satisfying decision, see *Lynn v. Nationwide Ins. Co.*, 2013 Pa. Super. LEXIS, at *704 (May 1, 2013) (permitting innocent co-insured coverage because of a recently passed state statute protecting innocent co-insureds, but not because of any relaxation of judicial formalism and hyper-textualism in policy interpretation).

1970s by adding beefed up business risk exclusions¹⁸⁷ as well as an asbestos exclusion,¹⁸⁸ an absolute or total pollution exclusion,¹⁸⁹ and a cap on the insurer's overall liability under the policy.¹⁹⁰ But the difficulty of these risks, particularly asbestos,¹⁹¹ may have made this inevitable. Although (relative to homeowners and other property insurance), the CGL policy still provides essentially broad coverage along the lines of Sawyer's

¹⁸⁷ See *supra* TAN 85–96 (discussing business risk exclusions).

¹⁸⁸ In the 1986 revision to the standard CGL form, the insurance industry added a broadly worded exclusion precluding coverage for liability claims in any way arising out of exposure to asbestos. Property insurance has since the 1980s similarly tended to expressly exclude coverage for repairs or retrofitting of property due to the presence of asbestos.

¹⁸⁹ Until the 1960s, the standard CGL form did not exclude coverage for pollution related claims, although some insurers were adding pollution exclusions to their policies. A 1970 form endorsement limiting pollution coverage came into widespread use and the industry in the 1973 revisions to the standard CGL form, which added a “qualified” pollution exclusion, so named because it excluded coverage for claims arising out of pollution discharge but qualified the exclusion with a significant exception that restored coverage if the discharge or release of the pollutant was “sudden and accidental.” These words became the subject of much litigation with insurers contending that to meet the exception the discharge must be swift or abrupt, while policyholders argued that the discharge (or even damage from the discharge) be only unintentional. Courts split on the interpretative question, prompting insurers in the 1986 revision to the CGL to include a broadly worded “absolute” pollution exclusion that barred coverage for any claim arising out a release or discharge, with the term “pollutant” broadly defined. A variant of this exclusion, often referred to as the “total” pollution exclusion, provides an exception where the claim or loss is due to smoke from a hostile fire. See generally, Stempel, *Reason and Pollution*, *supra* note 95.

¹⁹⁰ The 1986 CGL form also popularized use of an aggregate limit on coverage. Prior to this time, liability insurance was often sold with only limits on the amount the insurer would pay per occurrence, presenting the possibility that a policyholder faced with many sufficiently distinct claims could receive many times the stated policy limit. Under the modern CGL form with aggregate limits, the insurer's financial exposure is capped regardless of the number of claims against the policyholder.

¹⁹¹ The magnitude of the asbestos mass tort and its ripple effect on insurance is well-chronicled. See, e.g., *Asbestos: Anatomy of a Mass Tort*, *supra* note 121; Deborah R. Hensler, *Asbestos Litigation in the United States: Triumph and Failure of the Civil Justice System*, 12 CONN. INS. L.J. 255 (2006).

vision, it has also narrowed in scope¹⁹² and been plagued with enough uncertainty to create substantial coverage litigation and state-to-state variance regarding resolution of coverage disputes.¹⁹³

D. NARROWING AUTO INSURANCE

Likewise, automobile policies have tended to develop gaps or limitations on coverage, at least if much current coverage litigation is any indication. For years, auto policies tended to cover policyholders sued over a traffic accident so long as there was no significant evidence that the policyholder in fact intended to injure the third-party claimant. Short of ramming into another car out of spite, coverage was provided, certainly at the duty to defend stage where the question is whether a potential for coverage exists—and probably throughout the matter as well, so long as there was no evidence of subjective intent to injure.

Auto insurers have also added additional exclusions to their forms designed to avoid coverage for errant driving that arguably went beyond negligence, but stopped well short of the traditional intentional act limitations. Examples include exclusions for injury arising out of drunk driving or criminal acts. In some cases, criminal act exclusions have been construed literally against the policyholder and in favor of the insurer—exactly the opposite of the traditional doctrinal approach to bar coverage in cases of driver intoxication even in the absence of an express drunk driving exclusion.¹⁹⁴

¹⁹² See Kenneth S. Abraham, *The Rise and Fall of Commercial Liability Insurance*, 87 VA. L. REV. 85, 86 (2001); Kenneth S. Abraham, *Peril and Fortuity in Property and Liability Insurance*, 36 TORT & INS. L.J. 777 (2001).

¹⁹³ See MANILOFF & STEMPEL, *supra* note 95 (examining twenty-one prominent coverage issues and differing law of the fifty states on these issues).

¹⁹⁴ See, e.g., *McDaniel v. Sierra Health & Life Ins. Co.*, 53 P.3d 904, 905 (Nev. 2002) (enforcing criminal acts exclusion to deny death benefits to the named beneficiary in the case of an auto accident because policyholder was intoxicated and could have been prosecuted had he survived); see also Douglas R. Richmond, *Driving Drunk in the Serbonian Bog: Intoxicated Drivers' Deaths as Insurance Accidents*, 32 SEATTLE U. L. REV. 83 (2008); Michael E. Gardner, Note, *Accidental Death Insurance Coverage of Drunk Drivers*, 69 MO. L. REV. 235 (2004).

E. NATURAL DISASTERS AS EVIDENCE OF THE POVERTY OF THE FRAGMENTED APPROACH

The perils of the fragmented approach are most obvious after natural disasters such as hurricanes. After a storm such as Katrina or Sandy devastates an area, property insurance policyholders make claims. Whether the loss is covered typically hinges on whether the damage was sufficiently caused by either wind (a covered peril) or water (an excluded peril).¹⁹⁵ The all-or-nothing divide can tempt policyholders to fudge facts in an attempt to fit as much of a loss as possible under the covered category of wind. It can also tempt insurers to engage in sharp practices¹⁹⁶ that may even take on an aura of post-loss underwriting.¹⁹⁷ Even where a damaged home is covered by both

¹⁹⁵ See James A. Knox Jr., *Causation, the Flood Exclusion, and Katrina*, 41 TORT TRIAL & INS. PRACT. L.J. 901 (2006); Douglas R. Widin, *Katrina, Causation, and Coverage: Which Way Will the Wind Blow?*, 41 TORT TRIAL & INS. PRACT. L.J. 885, 885 (2006) ("It is no secret to even the casual observer of these events that the principal battle line will be over whether damage was caused by 'wind' or 'flood' within the terms of the policy, since the former is virtually always a covered peril and the latter is frequently excluded.").

¹⁹⁶ See Phil Gusman, *Sandy Impact 'More Severe' Than Irene; Interests Tie Storm to Larger Issues*, PROP. CAS. 360 (Oct. 30, 2012), available at <http://www.propertycasualty360.com/2012/10/30/sandy-impact-more-severe-than-irene-interests-tie> ("The Consumer Federation of America, meanwhile, criticized insurers' response to 2005's Hurricane Katrina and warned against a similar response to Sandy."); Chad Hemenway, *Mississippi Jury Finds State Farm Defrauded NFIP After Katrina*, PROP. CAS. 360 (Apr. 9, 2013), available at <http://www.propertycasualty360.com/2013/04/09/mississippi-jury-finds-state-farm-defrauded-nfip-a>.

¹⁹⁷ Post-loss underwriting, a term disfavored by insurers but used by policyholders, refers to insurer efforts to engage in hard-edged claims and coverage practices in an effort to avoid or minimize coverage for a policyholder, risk, or account that they in retrospect wish they had not agreed to underwrite by issuing the policy. See *Great Am. Ins. Cos. v. Subranni*, 332 B.R. 690, 727-29 (Bkrcty D. N.J. 2005) (regarding post-loss underwriting as unfair claims practices that insurer utilizes to avoid payment in connection with risk it now wishes it had not assume but rejecting policyholder's claim that insurer engaged in impermissible post-loss underwriting); Eugene R. Anderson, Richard G. Tuttle & Susannah Crego, *Draconian Forfeitures of Insurance: Commonplace, Indefensible, and Unnecessary*, 65 Fordham L. Rev. 825, 848, n.145 (1996) (characterizing post-loss underwriting as opportunistic behavior by insurer through sharp claims practices that seek to revise insurance arrangement in favor of insurer).

a homeowners' policy and a flood policy, there may still be disputes as each insurer attempts to place the bulk of coverage responsibility upon the other.¹⁹⁸ As discussed below, this situation is inefficient, unfair, and untenable.¹⁹⁹

The situation is further exacerbated by the failure of many agents and brokers to piece together the fragmented coverage available. Even when clients live within yards of an ocean, lake, river, stream, or wash, it appears that agents or brokers frequently advise them that they "don't need" flood insurance and can save the comparatively small premium cost that would have purchased the government-subsidized product.²⁰⁰ Sometimes this is because the intermediary has misread available flood mapping, though government maps of flood

¹⁹⁸ See, e.g., *J.R.A. Inc. v. Essex Ins. Co.*, 72 So. 3d 862 (La. Ct. App. 2011) (Katrina water/wind dispute); *Bayle v. Allstate Ins. Co.*, 615 F.3d 350 (5th Cir. 2010) (Katrina water/wind dispute); *Broussard v. State Farm Fire & Cas. Co.*, 523 F.3d 618, 624–25 (5th Cir. 2008) ("[A] stipulation that the Broussards' personal property was destroyed by Hurricane Katrina is insufficient to establish that it was destroyed by a windstorm, since Hurricane Katrina unleashed both wind and water forces."); *Gainer v. Specialty Risk Assocs., Inc.*, 977 So. 2d 1089 (La. Ct. App. 2008) (Katrina water/wind dispute).

¹⁹⁹ See Adam Scales, *A Nation of Policyholders: Governmental and Market Failure in Flood Insurance*, 26 MISS. C. L. REV. 3, 3 (2007) ("Our current systems for preventing, mitigating, and allocating these losses are fractured, diffuse, and maddeningly counterproductive."); Rachel Lisotta, Comment, *In Over Our Heads: The Inefficiencies of The National Flood Insurance Program and the Institution of Federal Tax Incentives*, 10 LOY. MAR. L.J. 511, 512–13 (2012). See also Charlene Luke & Aviva Abramovsky, *Managing the Next Deluge: A Tax System Approach to Flood Insurance*, 18 CONN. INS. L.J. 1, 1–5 (2011).

²⁰⁰ See Scales, *supra* note 199, at 7–21 (noting problem, exploring alternative explanations, and concluding that modern practice of selling and bundling mortgages has likely played a major role in underinsurance in that it diminishes the initiating lender's motivation to ensure that property is adequately insured). See, e.g., *Leonard v. Nationwide Mut. Ins. Co.*, 499 F.3d 419, 423, 425 (5th Cir. 2007) ("The Leonards' home lies twelve feet above sea level on the southern most edge of Pascagoula, Mississippi, less than two hundred yards from the Mississippi Sound. . . . [Nationwide agent Jay] Fletcher allegedly assured [Paul] Leonard that he did not need additional flood coverage because Leonard did not live in an area classified Zone A for flood risk by the Federal Emergency Management Agency ('FEMA').").

plains themselves may be of questionable accuracy.²⁰¹ Other times it is because the agent is correct in finding that the insured property is not in a flood plain, but mistakenly concludes that this is proof positive of the property's invulnerability from water damage risk.²⁰²

Whatever the circumstances, flood insurance is undersold to a surprising degree.²⁰³ One possible explanation is that agents do not earn enough commission on the comparatively low cost flood insurance premiums to properly incentivize them to sell

²⁰¹ See, e.g., *Nast v. State Farm Fire and Cas. Co.*, 82 S.W.3d 114, 118–19 (Tex. Ct. App. 2002) (“[In 1997,] Billie explained to [licensed agent Barbara] Taylor that she needed to talk about getting some flood insurance. After requesting Billie’s address, Taylor told Billie that she did not live in a flood zone. Billie replied, ‘Try telling my neighbors that. They had 18 inches of water in their house.’ Taylor then corrected herself by stating, ‘Well, you do live in a flood zone, but you do not live in the one that qualifies you for FEMA flood insurance.’ . . . In 1995, however, a bridge was constructed over Cibolo Creek, creating an obstruction in the waterway. As a result, the FEMA flood plains were redrawn. The new map indicated that the Nasts’ home was eligible for flood insurance.”).

²⁰² See, e.g., *Buente v. Allstate Ins. Co.*, 422 F. Supp. 2d 690, 697 (S.D. Miss. 2006) (“That is, I accept as true the plaintiffs’ allegations that they asked Allstate’s representatives whether they needed to purchase a flood insurance policy; that the Allstate representatives told them that the purchase of a separate flood insurance policy would not be necessary because their house was situated outside the flood plain and that all damage attributable to a hurricane, including damage caused by ‘storm surge,’ would be covered by the homeowners policy at issue.”); *Jones v. State Farm Gen. Ins. Co.*, No. 06-9874, 2007 WL 1428705, at *3 (E.D. La. May 11, 2007) (“[S]he was advised that, since the Delery Street property was in a no flood zone, that flood insurance was not necessary; plaintiff relied upon this advice and, therefore, did not have flood insurance on her property at the time water, from levee breaches, destroyed her home on or about August 29, 2005 . . .”); *Mladineo v. Schmidt*, No. 1:06CV1138 LTS-RHW, 2007 WL 1459445, at *1 (S.D. Miss. May 16, 2007) (“The concluding allegations are that ‘Schmidt also advised John that the property was not in a flood zone, and that a mortgage lender would not require a separate policy of flood insurance. Schmidt did not suggest that Plaintiffs obtain flood insurance.’”)

²⁰³ See Jeffrey Manns, Note, *Insuring Against Terror?*, 112 YALE L.J. 2509, 2510–11 (2003) (“The federal government has a long history of offering subsidized insurance programs, such as flood insurance, that are rife with moral hazards and have often served no one’s interests save the insured beneficiaries.”) (footnote omitted).

flood insurance.²⁰⁴ Indeed, they may have a problematic incentive to keep premiums lower by avoiding it so that they can offer their customers a total premium at or below that of competitors. If flood insurance were a mandated part of homeowners' and other first-party property coverage, much agent discretion—and with it much error—would be removed.²⁰⁵

Earth movement coverage presents a similar, but less vexing, fragmentation of property coverage. The typical consumer and commercial property policies bar coverage for earth movement, save for exceptions when the ground shifts due to a broken pipe or other more confined causes.²⁰⁶ Earth tremors or worse are effectively excluded, but additional coverage can be purchased for an additional premium so long as the policyholder accepts a high deductible or co-insurance of such claims.²⁰⁷ Because of the cost or lack of appreciation of the risk, most policyholders, even those in high-risk zones, pass on the opportunity to purchase

²⁰⁴ See Steven Plitt & Daniel Maldonado, *When Constitutional Challenges to State Cancellation Moratoriums Enacted After Catastrophic Hurricanes Fail: A Call for a New Federal Insurance Program*, 27 *BYU J. PUB. L.* 41, 85–86 (2012) (“As a result of catastrophic flooding which occurred along the Mississippi River in 1927, the private insurance industry abandoned the market for flood insurance. The catastrophic flooding jeopardized the solvency of many property insurers. The industry's aversion to flood risk stemmed from a variety of factors, including: ‘[p]oor, [i]nadequate, and [i]naccurate [i]nformation [a]bout [f]lood [r]isks;’ ‘[r]isk [c]orrelation;’ and ‘[a]dverse [s]election.’ . . . Regarding adverse selection, flood insurance presented a vexing problem whereby the people most likely to buy the insurance against flood losses were also the people most likely to suffer that type of loss.”).

²⁰⁵ See Scales, *supra* note 199, at 8–9.

²⁰⁶ See REJDA, *supra* note 18, at 164 (“Property damage from earth movement is excluded. This includes damage from an earthquake, shock waves from a volcanic eruption, landslide, mudslide or mudflow, subsidence or sinkholes, or earth sinking or shifting. However, an ensuing loss caused by fire or explosion is covered. An earthquake endorsement can be added to the policy.”); DORFMAN & CATHER, *supra* note 16, at 54, 97–98; VAUGHAN & VAUGHN, *supra* note 16, at 465–77.

²⁰⁷ See REJDA, *supra* note 18, at 164; DORFMAN & CATHER, *supra* note 16, at 54, 97–98; VAUGHAN & VAUGHN, *supra* note 16, at 465–77.

the coverage.²⁰⁸ There may also be underselling by agents and brokers.²⁰⁹

As a result, when earthquakes take place, most of those affected are effectively uninsured.²¹⁰ Although FEMA and other

²⁰⁸ See, e.g., *Approaches to Mitigating and Managing Natural Catastrophe Risk: H.R. 2555, The Homeowners' Def. Act Before the H. Comm. on Financial Services*, 111th Cong. 3 (2010) (statement of Glenn Pomeroy, Chief Exec. Officer, Calif. Earthquake Auth.) ("Frustrated in their efforts to control their earthquake exposure, insurers responded by severely restricting, or simply refusing to offer, sales of homeowners' insurance in the state, and with those efforts eventually reaching some 94% of the market, their actions threatened to deprive Californians of homeowners' insurance altogether."); Rick Swedloff, *Uncompensated Torts*, 28 GA. ST. U. L. REV. 721, 780 (2012) ("[I]ndividuals tend not to purchase insurance for high-risk, low-probability events. Individuals tend not to buy insurance against earthquakes, floods, hurricanes, or major medical events even when the government subsidizes the insurance such that the premiums are less than the expected loss. In both experimental settings and surveys, insurance purchasers act as if low probability results are unlikely to occur at all."); see HOWARD KUNREUTHER & MICHAEL USEEM, *LEARNING FROM CATASTROPHES: STRATEGIES FOR REACTION AND RESPONSE* 6–7 (Howard Kunreuther & Michael Useem et al. eds., 2010).

²⁰⁹ Although insurers have perhaps more commercial incentive to seek earthquake coverage than is the case with the federal government's flood program, there remains a strong incentive for agents to under-market earth movement coverage for fear that creating a higher priced product will lead to lost sales. Customers and prospective customers will take their business to other providers who offer a cheaper insurance package, even if that package is one that makes less sense in terms of sound risk management.

²¹⁰ See Jacqueline Young, Note, *Efficient Proximate Cause: Is California Headed for a Katrina-Scale Disaster in the Same Leaky Boat?*, 62 HASTINGS L.J. 757, 783 (2011) ("While the [California Earthquake Authority] is sound enough to withstand a 250-year earthquake event, to date, only twelve-to-thirteen percent of California homeowners have actually purchased earthquake insurance.") (footnote omitted) (citing *Approaches to Mitigating and Managing Natural Catastrophe Risk: H.R. 2555, the Homeowners' Defense Act: Joint Hearing on H.R. 2555 Before the Subcomm. on Hous. and Cmty. Opportunity and the Subcomm. on Capital Mkts., Ins. and Gov't Sponsored Enters. Of the H. Comm. On Fin. Servs.*, 111 Cong. 12–14 (2010) (testimony of Glenn Pomeroy, Chief Exec. Officer, Cal. Earthquake Auth.)); *Approaches to Mitigating and Managing Natural Catastrophe Risk: H.R. 2555, The Homeowners' Defense Act: Hearing on H.R. 2555 Before the Subcomm. on Hous. and Cmty. Opportunity and the Subcomm. on Capital Mkts., Ins., and Gov't Sponsored Enters. of the H. Comm. on Fin. Servs.*, 111th Cong. 4 (2010) (testimony of Glenn Pomeroy, Chief Exec. Officer, Calif. Earthquake Auth.) ("In earthquake-prone California, 88 percent—88 percent—of homeowners have no

government programs usually ride to the rescue with disaster aid, the current status quo is one in which an insufficient number of people with property at risk fail to get coverage, which in turn shrinks the risk pool and results in under-insurance and a post-quake system of compensation that essentially forces a massive taxpayer subsidy.²¹¹ If insurers instead provided comprehensive property coverage that included coverage for quakes, with apt premiums collected, the burden of post-quake repair could be more evenly distributed and solidly funded, with much less free-riding by large parts of the population at risk for quake-related losses.

V. REDISCOVERING THE SAWYER LEGACY AND RETURNING TO BROADER INSURANCE PRODUCTS

Sawyer and the other architects and supporters of the move from disaggregated liability coverage to the CGL format had an almost utopian vision, if that is possible in the sometimes mundane halls of business. The breadth of the CGL would

earthquake insurance at all. Increasingly, insurance companies are treating homeowners across the country like they have been treating Floridians for years, canceling policies and doubling or tripling rates in the wake of a single claim.”).

²¹¹ See Eric Lipton et al., *Flood Insurance, Already Fragile, Faces New Stress*, N.Y. TIMES, Nov. 13, 2012, at A1 (describing how claims have exceeded the \$3.5 billion annual premiums for the federal flood insurance program four out of the last eight years: “The fact that many homeowners hit by Hurricane Sandy have no flood or homeowners insurance could prompt Congress to provide assistance to the uninsured, too, as happened after Hurricane Katrina, further raising the cost to the federal Treasury.”), available at <http://www.nytimes.com/2012/11/13/nyregion/federal-flood-insurance-program-faces-new-stress.html?smid=pl-share>; see also Judith Kildow & Jason Scorse, Op-Ed., *End Federal Flood Insurance*, N.Y. TIMES, Nov. 29, 2012, at A31, available at <http://www.nytimes.com/2012/11/29/opinion/end-federal-flood-insurance.html?smid=pl-share> (claiming that taxpayers are “on the hook for at least \$527 billion of vulnerable assets in the nation’s coastal flood plains.”); Editorial, *U.S. Taxpayers Need Break from Underwater Flood Insurance*, BLOOMBERG, Nov. 11, 2012, available at <http://www.bloomberg.com/news/2012-11-11/u-s-taxpayers-need-break-from-underwater-flood-insurance.html>.

provide greater protection for both insurers and policyholders. It would protect insurers from information asymmetry: the risk of some policyholders purchasing only the insurance they were more likely to need, thus increasing claims relative to premium dollars (adverse selection). It would also resist the risks posed by moral hazard. Although every policyholder would be subject to the generic human tendency to be less careful if insured, at least the risk pool would be large enough and the premiums increased sufficiently through bundling that moral hazard would not have as much effect on the insurers' bottom line.²¹² Today, a similarly comprehensive approach across insurance offers the prospect of significant benefits to policyholders, victims, the public, and even to the insurance industry.

A. BENEFITS FOR POLICYHOLDERS

The CGL has benefitted policyholders by reducing gaps in coverage. It has provided increased funding for compensating victims, funding that has also improved and speeded dispute resolution and settlement. Other insurance products can also reflect the benefits of a more comprehensive approach. Most prominently, policyholders would benefit for many of the same reasons they benefitted from the CGL form. Gaps in coverage would be reduced.²¹³ Disputing costs prompted by the need to

²¹² I align with scholars who contend that the dangers of adverse selection and moral hazard are overstated. See Peter Siegelman, *Adverse Selection in Insurance Markets: An Exaggerated Threat*, 113 YALE L.J. 1223, 1261 (2004); Tom Baker, *On the Genealogy of Moral Hazard*, 75 TEX. L. REV. 237, 252–53 (1996); Ellen S. Pryor, *The Economic Loss Rule and Liability Insurance*, 48 ARIZ. L. REV. 905, 908 (2006); Luke & Abramovsky, *supra* note 199, at 31; Tom Baker, *Containing the Promise of Insurance: Adverse Selection and Risk Classification*, 9 CONN. INS. L.J. 371, 373–74 (2003). Particularly for policyholders that are flesh-and-blood individuals, it is a bit much to think that they will recklessly expose themselves to physical pain, death, or the destruction of their abodes or most precious belongings simply because they are insured. Consequently, the moral hazard risk posed in selling life, health, homeowners', and auto insurance logically is not all that great. I am not suggesting moral hazard is not an important concern, but it may not be nearly as important as traditionally theorized.

²¹³ Policyholders would correspondingly be more likely to find that actually available insurance coverage conforms to their pre-loss expectations of coverage. See James Davey, *Fracturing and Bundling Risks: The Coverage*

characterize losses for coverage purposes would be reduced. Policyholders would be protected from their own cognitive errors in failing to appreciate either the need for sufficient insurance coverage or engaging in penny wise/pound foolish behavior by unwisely forgoing coverage simply to save a modest amount in premiums.

A classic example of the opportunity for large social gains through consolidation is the staple homeowner's policy. As discussed above, the dangers of disaggregation were laid bare in the coverage litigation related to Hurricane Katrina losses. Despite the pain of that episode, it is likely to be replayed again through coverage litigation in the wake of Hurricane Sandy or storms taking place during 2013. Once again, we will be treated to protracted litigation over whether losses were caused primarily by wind or water. We have seen this movie before and it gets no better with age.

Instead of continuing to stumble along in this area through a quilt of fragmented coverage, insurers should move, or courts and regulators should force them to move, toward more inclusive coverage. A homeowners' policy should include not only the array of fire, wind, and vandalism coverage found in the HO-3, but also include flood and earthquake insurance. Like the CGL, this type of comprehensive homeowners' coverage will provide needed protection to policyholders while greatly reducing disputing costs.

Adam Scales has already made a compelling case for mandated flood coverage.²¹⁴ His argument seems to me unassailable, yet there has been no progress toward this during the eight years since Katrina. Instead, the limited legislative activity has revolved around whether to continue the federal flood insurance program and on what terms.

The typical homeowner's policy expressly excludes flood coverage. If you want flood coverage, you need to purchase it

Expectations of the "Real" Reasonable Policyholder, 11 RUTGERS J. L. & PUB. POL'Y ____ (2013) ("[h]uman beings are often poor judges of risk" and thus are vulnerable to underinsurance as well as likely to expect coverage though without significant scrutiny of policy provisions).

²¹⁴ See Scales, *supra* note 199; see also Kunreuther & Pauly, *supra* note 63 ("Fewer than half the residents in flood and hurricane-prone areas were insured against water damage from Hurricane Katrina and Hurricane Sandy.").

through the federal government's program that, notwithstanding its existence as a federal program, involves purchase of the coverage through the agent selling homeowners' coverage. As discussed above, agents have been shockingly reluctant to push clients to purchase the flood coverage, even when the property at issue is close to the sea, rivers, or other bodies of water. Explanations vary from outdated or inaccurate flood plain maps, simple ignorance (e.g., the agent who thinks that a property outside a flood plain is invulnerable), consumer cognitive error (e.g., policyholder reluctance to pay a higher premium for contingent protection when the risk is seen as too remote), misaligned incentives (the agent earns less commission with a flood insurance sale and thus invests less effort in making the sale), or inadequate monitoring by stakeholders (mortgage lenders sell notes downstream to financiers so quickly that no lender with a close connection to the community has adequate incentive to insist that property be adequately insured).²¹⁵

Whatever the reason, there is no question that flood insurance is undersold. Requiring all homeowners' policies to provide the coverage would slice this Gordian Knot. Insurers and some policyholders outside flood-prone areas object on grounds this would needlessly increase premiums for some. On closer analysis, the objection is not compelling. First, although property closer to the ocean is generally at greater flood risk than inland property, the imbalance is not as dramatic as commonly supposed. Inland rivers flood with considerable frequency and ferocity. Floods in the Red River Valley along the North Dakota-Minnesota border provide a particularly good example of flood damage a long way from the ocean.²¹⁶ Similar havoc frequents Wayne, New Jersey, which is inland some

²¹⁵ See Scales, *supra* note 199, at 7–21 (addressing potential explanations for under-purchase of flood coverage). See also *id.* at 13–17 (describing National Flood Insurance Program, which although revised since 2006 has same fundamental characteristics); see also *supra* TAN and notes 214–23.

²¹⁶ See generally Douglas C. Friez & Kathleen Donahue, *North Dakota After Action Report: A Historical Perspective*, 2 GREAT PLAINS NAT. RESOURCES J. 193 (1997); see also Joshua P. Fershee, *The Rising Tide of Climate Change: What America's Flood Cities Can Teach Us About Energy Policy, and Why We Should Be Worried*, 39 ENVTL. L. 1109 (2009).

twenty miles from the sea, causing significant losses.²¹⁷ Tallahassee, Florida is a long way from the beaches normally associated with the state. Indeed, there is no river of consequence nearby. But in 1995, entire neighborhoods flooded simply from unusually heavy rains that overwhelmed the slow-draining red clay soil.²¹⁸ Flooding is not just a coastal problem.

Of course, some insurers will undoubtedly counter that whether coastal or inland, flooding risk differs across the country. To state a truism, property on high ground is less susceptible to flooding wherever it is located geographically. When policy debate is posed as a rhetorical question, we can (and probably should) ask why a homeowner on a hill overlooking Aspen, Colorado should have to pay a higher premium for flood coverage more likely to be invoked by a policyholder with a farm in the Missouri River Valley or a beach house in Pensacola, Florida.²¹⁹

To me, the answer is fairly obvious. Aspen aeries may not flood as much (although some properties on even seemingly high ground can be flooded based on drainage patterns that

²¹⁷ See Marc R. Poirier, *Takings and Natural Hazards Policy: Public Choice on the Beachfront*, 46 RUTGERS L. REV. 243, 324 n.285 (1993) (discussing chronic flooding in Wayne, N.J. and the proposed response); Laura Incalcaterra, *Ramapo Watershed Council Outlines River-Protection Efforts*, THE JOURNAL NEWS, April 20, 2007, at 1B (“But Wayne has long had a flooding problem, mainly because it is nearly surrounded by the Passaic, Pompton and Ramapo rivers.”).

²¹⁸ See Ronald Smothers, *Hurricane Slams into Florida with Winds of 145 M.P.H.*, N.Y. TIMES, Oct. 5, 1995, at B16 (“Tom Roche, the emergency planning director for Santa Rosa County, said the wind was whipping trees, tossing signs about and causing widespread flooding in the area.”); see also Kevin Sack, *Storm Leaves a Tapestry of Ruin on Florida Panhandle Beaches*, N.Y. TIMES, Oct. 6, 1995, at A1.

²¹⁹ Although, it should be remembered that mandatory flood coverage in the homeowners’ policy does not mean that all policyholders will pay the same premium for this more comprehensive, less fragmented coverage. Insurers would remain free to charge higher premiums to lowland homes than highland homes and would likely do so. The apt actuarial calculation of these different premiums for these different exposures lies beyond the scope of this article. But it should be noted that highland properties may pose different risks that even-out the overall exposure of the insurer. For example, homes in the California hills face significant wildfire risk absent from most waterfront homes.

laypersons are ill-equipped to detect), but they probably produce many more frozen pipes, snow-caused roof collapses, and wildfire losses than a beach house on the Gulf Coast or a three-bedroom rambler in Phoenix. Aggregate these different risks across the Snowbelt, areas of higher crime, earthquake zones, Tornado Alley (the area of the American Midwest frequented by tornadoes in Spring and Summer), and the like, as well as coastal and low-lying country, and it becomes less clear which way runs the subsidy. If something as basic as homeowners' insurance is broadened through required coverage and larger aggregations of risk, there may be some intra-pool subsidization of policyholders, but so what?

The very nature of the aleatory insurance product makes it something of a gamble for both sides, albeit a wager worth making. A policyholder may pay years of premiums without ever having a claim of any type. Is this unfair? Hardly. Protection has been received should it ever have been needed. The policyholder still obtained that for which he paid. Even if one were to classify the claimless policyholder as a "loser" in the transaction because it never suffered a loss that triggered a right to be indemnified (for the loss, most sane policyholders would just as soon wish it never had happened), this would not undermine the wisdom of requiring broader coverage to provide broader protection, and the risk management and disputing efficiencies flowing from a less fragmented approach.

Whether premiums may have been slightly higher because of bundled coverage is not nearly as important a financial issue to this "disappointed" policyholder as the fact that he paid premiums for what he wrongly views as nothing in return. Had there been one or more claims under the policy, the additional premiums paid over the years would likely be miniscule in relation to the indemnity benefits received in connection with even a single serious loss claim.²²⁰

²²⁰ The "endowment effect" is a tendency to which most humans are susceptible and seems to strengthen this common sense observation. People have a tendency to place greater value on what they already have than they do on the same object prior to purchase. For example, test subjects regularly state that they are willing to pay X for an object but then as soon as they own it regularly demanded X + quite a bit more as the price for selling it. See CASS R. SUNSTEIN & RICHARD THALER, *NUDGE: IMPROVING DECISIONS ABOUT HEALTH, WEALTH, AND HAPPINESS* 83 (2008); see also WARD FARNSWORTH, *THE LEGAL*

To be sure, there is a price break point of sorts that would make me think twice before advocating mandated flood coverage, earthquake coverage, replacement cost indemnification, and the elimination of other exclusions or coverage deductions. If homeowners' premiums were to double or triple, the case for consolidating all risks into one policy would need rethinking.²²¹ But this is unlikely. Consider a typical Sun Belt homeowner with a \$250,000 house paying roughly \$1,200 per year, perhaps less, for an HO-3 policy that lacks flood and earthquake insurance. Adding this coverage is likely to increase premiums perhaps as much as 10–20%, but not 100%.²²² And although \$250 is not a trivial sum, neither is it a

ANALYST: A TOOLKIT FOR THINKING ABOUT THE LAW 209–10 (2007); BEHAVIORAL LAW AND ECONOMICS 223–25, 261 (Cass R. Sunstein ed., 2000). Consequently, the policyholder will place a greater than rational value on the home or other property owned, and presumably would prefer to protect it even at the cost of paying higher premiums over the years. The effect may be a bit muted in that the money used to pay premiums is, of course, also the policyholder's money (although not necessarily, as sometimes premiums are financed). But it appears that the endowment effect applies to objects, but not to the more readily fungible wealth of cash. See Daniel Kahneman, Jack L. Knetsch & Richard H. Thaler, *Experimental Tests of the Endowment Effect and the Coase Theorem*, in ADVANCES IN BEHAVIORAL ECONOMICS 55–74 (Colin F. Camerer, George Loewenstein & Matthew Rabin eds., 2004).

²²¹ But even an enormous increase in premiums charged for insuring high risk properties (e.g., the “McMansion” on the beach) is an arguably acceptable cost of better linking insurance costs to the actual risks presented. Perhaps most important, a spike in property insurance premiums that creates a new normal does not mean that rates will continue to skyrocket. More likely, they will stabilize after the spike. Going forward, the newly normal higher rates for high risk property will make for a better informed, more efficient market regarding the pricing of such properties and insurance on them.

²²² We know, for example, that flood insurance is relatively inexpensive, with typical flood premiums running at only a small amount (10–15%) relative to the premium on an entire owners' or renters' policy. Earthquake coverage, which lacks the government backing enjoyed by flood insurance, also adds only a relatively small percentage of the overall policy premium (although the coverage has a higher deductible than other components of the homeowners' policy). Thus, even if there was no economy of scale from requiring flood and earth movement coverage as a part of the standard homeowner or business property policy, the net increase in premium cost would likely be something on the order of 25% if the national government wishes to continue to subsidize flood losses. Although policyholders in outside high risk flood and earthquake zones might complain, they would be forced to accept paying for this more

substantial additional burden upon this solidly middle class citizen in return for both his own greater protection (earthquakes do happen in Nevada and Arizona as well as California, and desert washes²²³ occasionally overflow or breach

comprehensive coverage, which in turn, they might need someday. That will in any event lead to sounder risk management and disaster compensation far less dependent on FEMA and related post-catastrophe remedial action by the government that is funded by general taxpayer revenues.

Of course, continued government subsidy of flood loss may be bad public policy. In addition to generally encouraging excessive development of coastal and waterfront areas, it certainly encourages purchase of such property in circumstances where the purchasers might well decline if they were forced to pay the true cost of waterfront ownership. *See* Hornstein, *supra* note 9. Even under the current situation of subsidy for flood insurance, homeowner insurance premiums have risen more than 50% in Gulf Coast states, with hurricane victims self-insuring for 15–20% of losses in 2004; if flood premiums were completely market-based, cost to waterfront homeowners could approximate \$30,000 per year, subject to reduction to range of \$3,500–\$7,000 per year for building at higher elevation or taking other preventive measures, such as raising the existing structure.

In commentary at the Conference, Dr. Weisbart suggested that increases of this type are so large as to undermine my argument in favor of mandating flood and water damage coverage in homeowner policies and in favor of more integrated, non-fragmented coverage. Even under a worst-case analysis, I am not sure I would agree. Someone who builds a McMansion almost at the water's edge probably should pay the market rate of insurance and internalize the full cost of being this type of high-end property owner. More likely, however, is something other than a worst case analysis. If flood coverage is part of all homeowner coverage, there will be some subsidization of the waterfront owner by the owners of three-bedroom ramblers in midwestern suburbs, although some of this will be muted by additional underwriting and imposition of additional premiums. Return subsidies may come from a waterfront owner to suburban Midwesterner in the wake of ice storms, tornadoes, and frozen pipes. To the extent a subsidy takes place, my position is that it is a necessary evil to have more coherent insurance coverage for natural disasters.

In response to a particular Weisbart criticism wondering whether I propose that flood coverage be mandatory in renters' policies, the answer is a resounding "yes." Renters insurance is cheap, even for starving college students. Mandating comprehensive coverage—and it must be mandated so that cut-rate insurers do not unfairly underprice more comprehensive policies—is not likely to add much to the cost of such policies.

²²³ For the benefit of readers who do not reside in the Southwestern U.S.: a "wash" is a normally dry river or creek bed that contains run-off water (that can fill or even overflow the wash) after a rainstorm. Regarding earthquakes, although the Western U.S. generally experiences more tremors, the New Madrid Fault, which passes through the heartland of the nation, is viewed by geologists

aging walls) and as part of a sounder national risk management policy.

Those complaining that mandated inclusive coverage forces cross-subsidization of policyholders overlook the cross-subsidization that takes place today in the aftermath of natural disasters. The same policyholders with property on high ground or well away from fault lines may have paid lower premiums for their homeowners' insurance, but they surely pay tax dollars used to deliver emergency aid to disaster victims who lack flood coverage, earthquake coverage, or full indemnity protection.²²⁴ Even if broadened coverage results in higher premiums that are seen as unfair to property owners facing lower risk, the net cost of a new system may be lower overall, and would likely place less of a drain on government resources by shifting much of the risk to the private sector. The U.S. government heavily subsidizes today's federal flood insurance program²²⁵—and that subsidy is financed by the same taxpayers who are also policyholders.

In proposing broader coverage, I am not suggesting that insurers offer the additional coverage at cut-rate premiums. Insurers should be permitted to charge fair market-based premiums and—within reason—to make distinctions based on

as a likely future source of significant earthquakes that would do most of their damage in the South-Central U.S. and possibly the Eastern Seaboard. If this occurs, everyone will be quite happy that the nation prepaid the costs of such losses through widespread mandatory insurance and years of accumulated premiums.

²²⁴ See *Congress Passes \$50.5B Superstorm Sandy Aid Bill*, WASH. POST, Jan. 29, 2013, http://www.washingtonpost.com/politics/congress-passes-505b-superstorm-sandy-aid-bill/2013/01/28/99a13262-69ab-11e2-95b3-272d604a10a3_story.html; David Lawder, *Senate Approves \$50.5 Billion in Long-Delayed Superstorm Sandy Aid*, REUTERS, Jan. 28, 2013, <http://www.reuters.com/article/2013/01/29/us-usa-congress-sandy-idUSBRE90R10620130129>.

²²⁵ See RAWLE O. KING, CONG. RESEARCH SERV., R42850, THE NATIONAL FLOOD INSURANCE PROGRAM: STATUS AND REMAINING ISSUES FOR CONGRESS 17 (2013), available at <http://www.fas.org/sgp/crs/misc/R42850.pdf> ("The NFIP was self-supporting from 1986 until 2005, covering all administrative expenses and claim payments out of premium income and fees. Since Hurricane Katrina struck in August 2005, FEMA has had to borrow \$19.64 billion, which includes \$2.6 billion over the 2007-2009 period, to pay claims from Hurricane Ike and the Midwest floods of 2008.")

the risks presented. Recipients of broad coverage in Florida may need to pay significantly more than those in Nebraska if, as an actuarial matter, the Florida homes face greater risk of loss overall from the totality of perils covered pursuant to bundled coverage.

Similarly, insurers can protect themselves and help reduce premium costs by requiring higher deductibles or co-pay requirements for certain difficult risks. Today's common norm of a higher deductible for earthquake coverage, which tends to be available for the property insurance policyholder willing to pay for it even if flood coverage is not absent the federal program, makes sense as a means of risk-sharing between policyholder and insurer. The key is that such measures be reasonable and actually necessary for protecting insurance risk pools rather than being a means by which insurers simply build capital without providing sufficient protection to policyholders.

One criticism of the comprehensive approach is that it creates a product that is too expensive for many, particularly those of low or moderate income. At the risk of sounding unsympathetic, I am relatively unmoved by this argument. For decades, the minimum amount of automobile insurance has been low (\$15,000 per claimant/\$30,000 per accident in some states). Although this reduces the premiums paid by the poor and the frugal, it has produced decades of unnecessary litigation (both tort claims and underinsured motorist claims) when victims are unable to receive adequate compensation from tortfeasors with such minimum policy limits. Higher limits would increase insurance costs, which would fall more heavily on those with less wealth, but the amounts are not so large as to be insurmountable; forcing purchase of adequate insurance would bring the benefit of forcing those who want to drive to pay their way for the privilege, which may in turn have the collateral benefit of reducing driving and attendant energy and environmental costs. Mandating sufficiently comprehensive insurance would likely have similar positive impact for society as a whole sufficient to overcome the inconvenience or hardship imposed on the poor.²²⁶

²²⁶ See Kunreuther & Pauly, *supra* note 63 (unduly low premiums or inadequate coverage forces taxpayer-funded aid in the wake of catastrophe). At the risk of sounding unduly Republican about this, I also note that many cries of excessive poverty are ill-taken. People routinely say that they "can't afford" to

B. BENEFITS FOR VICTIMS

Liability insurance is acknowledged to have many purposes other than protecting policyholders and insureds from the burden of defending claims and the consequences of liability. It also serves to provide a means of compensating victims, as well as a socio-economic function in assisting with risk management and mitigating the consequences of injuries.

Individual tortfeasors, like errant drivers, are often without the financial resources to remedy the consequences of their actions. Consequently, if not for liability insurance, these impecunious drivers would be without means to compensate their victims. Even a middle class tortfeasor often has few liquid assets,²²⁷ and, thus, obtaining compensation would involve

pay a socially useful cost such as taxes, user fees for parks or athletic facilities, etc. But many of these same people manage to purchase alcohol, cigarettes, multiple daily cappuccinos, a vehicle more expensive than necessary for their transportation needs, new clothing, and—perhaps most infamously—homes with unrealistically high mortgage payments.

The housing collapse of 2008/2009 illustrates the harm that can occur when vendors are unwilling to act as gatekeepers or at least price products appropriately. Just as some of the earliest twenty-first century home purchasers would have been better off being denied a mortgage and making a more modest purchase or renting rather than buying, many consumers and businesses will benefit from being forced to purchase adequately comprehensive insurance, even if this means redirecting additional amounts of their income toward payment of premiums. In similar fashion, government and market failure to require adequate environmental care due to lack of will or fears of stifling economic growth often carry a long-term cost far greater than would have been the regulatory burden. *See, e.g.,* Edward Wong, *Life In A Toxic Country*, N.Y. TIMES, Aug. 4, 2013, http://www.nytimes.com/2013/08/04/sunday-review/life-in-a-toxic-country.html?_r=0 (describing how pollution and inadequate food safety not only impose psychological costs, but also result in wasteful and inefficient economic behavior prompted by efforts to mitigate safety problems created by lack of regulation).

²²⁷ *See* Allison K. Hoffman & Howell E. Jackson, *Retiree Out-of-Pocket Healthcare Spending: A Study of Consumer Expectations and Policy Implications*, 39 AM. J.L. & MED. 62, 64 n.9 (2013) (“Studies report savings shortfalls, healthcare costs as exacerbating retirement risk (defined as a substantial and detrimental decrease in standard of living) or healthcare costs consuming a large portion of household assets.”); *see also* Annie Duflo & Dean Karlan, *Changing Savings Habits*, STANFORD SOC. INNOVATION REV., 2012, at 7, available at http://www.ssireview.org/pdf/Fall_2012_Changing_Savings_Habits.pdf (“We’ve overborrowed, with average credit card debt more than

executing on real or tangible personal property or garnishing wages. Liquid assets such as savings accounts or brokerage accounts can be located and executed upon, but only with some effort.²²⁸ This is because a determined tortfeasor judgment debtor may be able to hide or immunize assets.²²⁹ For example, filing for bankruptcy often permits the discharge of the debtor's personal liability.²³⁰ Although when an individual or business files for bankruptcy the insurance policy is technically considered a part of the debtor's estate, it remains available to pay claims as needed, thus protecting the debtor (without diminishing the size of the estate for purposes of attempting to satisfy commercial obligations) and tort victim claimants, who might otherwise find the debtor without sufficient assets to provide compensation.²³¹

\$5,000; and 50 percent of Americans haven't adequately saved for retirement.").

²²⁸ See generally DAVID F. HERR, ROGER S. HAYDOCK & JEFFREY STEMPEL, FUNDAMENTALS OF LITIGATION PRACTICE chs. 1, 30 (2013 ed.) (describing the execution process after obtaining a judgment).

²²⁹ See Lynn M. Lopucki, *The Death of Liability*, 106 YALE L.J. 1, 14–32 (1996) (describing vast range of options debtors may have for secreting assets or removing them from the reach of creditors).

²³⁰ See WILLIAM L. NORTON, JR. & WILLIAM L. NORTON III, NORTON BANKRUPTCY LAW AND PRACTICE § 58:1 (3d ed., 2010). The basic purpose of the bankruptcy system is to provide debtors with the opportunity for an economic "fresh start." *Id.* at 58-2. "The most significant element of the 'fresh start' concept is the discharge of the debtor's personal liability for debts. In fact, in most consumer Chapter 7 cases, the prospect of discharge of existing liabilities is the major, if not the only, goal of the debtor." *Id.* at 58-2–58-3. In a Chapter 13 bankruptcy case, 11 U.S.C.A. § 1328(a) discharge is available only after completion of all payments under the plan, a process usually satisfied when the debtor makes all the required payments to the trustee as part of confirmed plan. *Id.* at 58-5. However, discharge provided by § 1328(a) does not include any debt "for restitution or a criminal fine," including debts from drunk driving under § 523(a)(9). *Id.* at 58-5 n.11.

²³¹ See *In re Titan Energy, Inc.*, 837 F.2d 325 (8th Cir. 1988) (although product liability insurance policies were considered property of the debtor's estate, available policy proceeds in connection with covered claims do not flow into the estate but are paid to product liability claimants); *Louisiana World Exposition, Inc. v. Fed. Ins. Co.*, 832 F.2d 1391 (5th Cir. 1987) (same re directors & officers liability insurance of debtor); Appleman on Insurance § 3342; Barry L. Zaretsky, *Insurance Proceeds in Bankruptcy*, 55 Brook. L. Rev. 373 (1989).

For commercial tortfeasors, liability insurance may permit a reputable business to continue to flourish by curtailing the potential for liability claims to attach to their assets—a major goal of liability insurance. Although these commercial policyholders have the wealth to pay settlements and judgments, as with individual financially stable tortfeasors, issues of access to funds often present themselves. Even successful businesses may not have the cash flow or liquidity to pay large or numerous liability claims in a timely fashion. Insurance gives victims of commercial tortfeasors more ready access to compensation without disrupting the business of the commercial policyholder.

First-party insurance protects victims of mishaps because the first-party policyholder and other insureds are also victims of fire loss, wind loss, theft loss, and the like. The loss of property of course most acutely affects the property owners, but it also affects those in the community connected to the property such as suppliers of a business, customers, or even lawn, pool, and domestic workers connected to an individual's residence. The sooner damaged property is restored and operations resume, the better off are these impacted parties. To the extent the absence of insurance or inadequate insurance retards the rebuilding process, these constituencies suffer injury. And although it may not be as concrete an injury, neighbors and the local community are aesthetically and psychologically injured when eyesore-like property damage remains unrepaired for longer than necessary.

C. BENEFITS FOR THE PUBLIC AND THE PUBLIC INTEREST

Even if insurance did nothing more than protect its policyholders, assist in the management of claims, and provide victim compensation, it would serve the public interest in multiple ways. Consider liability insurance. When a victim is injured, there are collateral costs externalized to society as a whole, such as medical expenses and costs associated with police, fire, and other government services. Additionally, traffic is disrupted; productivity is diminished; and the general spirit of

the community may suffer, particularly if property damage is widespread, or if the damaged property is crucial to local operations or infrastructure (e.g., a town hall, church, or basketball arena).²³²

In addition to compensating the victim, both liability insurance and first-party insurance compensate vendors, who may have provided help through features like the medical payments provisions of auto insurance policies as well as medical, disability, and life insurance. By providing funds for health care professionals and compensating for lost economic activity, insurance will help the victim and his or her family, employer, and community.

To the extent that insurance is not available for a loss, the costs associated with it are more likely to be externalized.²³³ Again, flood risk provides a good example. As discussed above, because flood insurance must be purchased separately, there is too little in place relative to the risks of flood damage. The national government provides significant subsidization of flood insurance coverage.²³⁴

When floods affect uninsured property, the victims predictably turn to the government for disaster relief. In effect, FEMA relief and related assistance in the wake of a flood, hurricane, or other major storm provide a backstop insurance program funded not by its beneficiaries, but by taxpayers generally, regardless of their risk profile.²³⁵ Having such

²³² The many ways in which insurance permeates society are well-chronicled. *See generally* RICHARD V. ERICSON, AARON DOYLE & DEAN BARRY, *INSURANCE AS GOVERNANCE* (2003). *See also* Shauhin Talesh, *Insurance Law as Public Interest Law*, 2 U.C. IRVINE L. REV. 985, 992–1005 (2012); Jeffrey W. Stempel, *The Insurance Policy as Social Instrument and Social Institution*, 51 WM. & MARY L. REV. 1489, 1495 (2010).

²³³ *See, e.g.*, Marty Schladen, *West, Texas blast reveals lack of insurance rule*, EL PASO TIMES, May 5, 2013, http://www.elpasotimes.com/ci_23169464/blast-reveals-lack-insurance-rule (noting problems posed by lack of adequate insurance covering fertilizer plant that exploded in West, Texas, on April 17, 2013).

²³⁴ *See supra* TAN 203–213.

²³⁵ *See* Scales, *supra* note 199, at 3–7. *See generally* Kunreuther & Pauly, *supra* note 63.

protection funded on an ongoing basis by those who will benefit from such programs of de facto “coverage” would be an improvement of both efficiency and equity by requiring those who benefit to contribute to a system of risk distribution and rebuilding.

Insurance serves the public interest to the extent insurers work to reduce losses that harm society. History provides several examples of the insurance industry pursuing underwriting practices or political goals that made the world safer or less wasteful. Underwriters Laboratories, as the name implies, began as a property insurer’s effort to encourage safer appliances.²³⁶ Risks such as overheating coffee pots or frayed lamp cords, which once caused substantial fire damage, are now comparatively rare because of the improvement in the safety of electronic products that began with Underwriters Laboratories.²³⁷

²³⁶ Concerned about the number of fires started by malfunctioning appliances, property insurers during the early 20th century created an organization for testing lamps and other products, resulting in enhanced attention to safety by manufacturers seeking to receive approval from Underwriters Laboratories. This approval was important, as it meant that companies could display the “UL” label, a symbol of safety, on their products. See *Underwriters Laboratories, Inc. History*, FUNDING UNIVERSE COMPANY PROFILE DATABASE, <http://www.fundinguniverse.com/company-histories/underwriters-laboratories-inc-history/> (last visited Nov. 7, 2013); see also *History*, UNDERWRITERS LABORATORIES, <http://www.ul.com/global/eng/pages/aboutul/history/> (last visited Nov. 7, 2013).

²³⁷ See Donald R. Ballman, Comment, *Software Tort: Evaluating Software Harm by Duty of Function and Form*, 3 Conn. Ins. L.J. 417 (1996) (“The insurance industry has a long history of encouraging its insureds to minimize their exposure to third party claims. The famous Underwriters Laboratories, best known for their ubiquitous UL symbol on manufactured products, was created as a joint venture of several insurance companies as a means of testing the quality of the products which their insureds produced. Because higher quality products posed less risk exposure, the insurers could pass along a portion of their savings to the insureds via reduced premiums. The consuming public enjoyed higher quality products, less risk of injury and prices moderated at least in part by the lower premiums the manufacturer[s] were required to pay. More recently, insurance companies have instituted “loss control” programs in which insurance specialists work closely with insureds to identify and eliminate avoidable exposures for business claims, property claims and the like.). But see Peter Molk *The Puzzling Lack of Cooperatives*, 88 Tulane L. Rev. 18 n.81 (forthcoming 2014), available at http://papers.ssrn.com/sol3/papers.cfm?abstract_id=2263480 (noting the modern trend of insurers

Seat belts and air bags, both of which were supported by the insurance industry²³⁸ before they were embraced by automakers or the body politic, have helped reduce the number of vehicle-related deaths in half, as well as reduced vehicle-related injuries generally, even as the population has grown by tens of millions since the initial mandated use of these devices in 1968 and 1980, respectively.²³⁹ Today, insurers have been important supporters

paying less attention to loss reduction and more attention to loss prediction and minimization of their exposure to risk). *See also* Frank Partnoy, *Barbarians at the Gatekeepers?: A Proposal for a Modified Strict Liability Regime*, 79 Wash. U. L.Q. 491, 507 (“UL has not survived and prospered during the last century exclusively because of its reputation for quality; instead, it has derived great value from monopoly property rights based on regulatory requirements and preferences related to UL labels.”) (footnote omitted). But Professor Partnoy also notes that his “argument is not that UL labels necessarily are inaccurate; instead, it is that UL’s dominance is only partially sustained by its reputation for quality certification.” *See* 79 Wash. U. L.Q. at 508.

²³⁸ *See* Robert Kneuper & Bruce Yandle, *Auto Insurers and the Air Bag*, 61 J. RISK & INS. 107, 107 (1994) (“Of particular interest were the opposing positions taken by automakers, who preferred mandatory seat belt laws, and auto insurers, who preferred a passive restraint mandate.”); *see also* Joan Claybrook & Benjamin Kelley, *Air Bags for All Cars*, N.Y. TIMES, July 30, 1991, available at <http://www.nytimes.com/1991/07/30/opinion/air-bags-for-all-cars.html> (“At the behest of insurers and safety groups, the Supreme Court in 1983 ordered an end to the ‘regulatory equivalent of war against the air bag’”); *see also* Richard W. Stevenson, *Insurance Reform in a Deadlock*, N.Y. TIMES, Sept. 23, 1991, available at <http://www.nytimes.com/1991/09/23/business/insurance-reform-in-a-deadlock.html?pagewanted=all&src=pm> (“On both the national and state levels, insurers and consumer groups are banding together to help control costs by pushing for more stringent safety laws, including lower speed limits and stricter enforcement of seatbelt laws, and by lobbying for other mutually beneficial changes like stronger bumpers.”).

²³⁹ *See* NAT’L HIGHWAY TRAFFIC SAFETY ADMIN., U.S. DEP’T OF TRANSP., TRAFFIC SAFETY FACTS: 2011 DATA (2013), available at <http://www-nrd.nhtsa.dot.gov/Pubs/811729.pdf> (use of seat belts and airbags have resulted in substantial reduction of driving-related deaths and injuries). (“Research has found that lap/shoulder seat belts, when used, reduce the risk of fatal injury to front-seat passenger car occupants by 45 percent and the risk of moderate to critical injury by 50 percent. For light-truck occupants, seat belts reduces the risk of fatal injury by 60 percent and moderate-to-critical injury by 65 percent;” Among passenger vehicle occupants age 5 and older, seat belts saved an estimated 11,949 lives in 2011.”) (p. 4 of *Occupant Protection* section of Traffic Safety Facts) (“Frontal air bags, combined with lap/shoulder belts, offer effective safety protection for passenger vehicle occupants. NHTSA analyses indicate a fatality-reducing effectiveness from frontal air bags of 14 percent

of measures to limit or forbid cell phone use while driving, particularly through public awareness campaigns.²⁴⁰ Where insurers take on risk, they have a strong incentive to reduce it, which, in turn, can increase consumer and public safety. For example, one recent study found significant insurer impact in reducing risk associated with consumer goods, food safety, and financial statements.²⁴¹

when no seat belt was used and 11 percent when a seat belt was used in conjunction with frontal air bags;" In 2001, an estimated 2,204 lives were saved by frontal air bags. From 1987 to 2011, a total of 34,757 lives were saved") (p. 5 of *Occupant Protection* section of Traffic Safety Facts). See also NHTSA, Traffic Safety Facts: 2008 Data, *Overview* (altos available at NHTSA website) at p. 3 (fatality rate per million vehicle miles travels has fallen from 1.58 in 1998 to 1.27 in 2008, a time during which the number of states mandating seat belt use and enforcing seat belt use laws grew to 2008 figure of 49 states and D.C.) ("From 1975 through 2008, NHTSA estimates that seat belts saved 255,115 passenger vehicle occupants age 5 and older, including 13,250 lives saved in 2008.").

²⁴⁰ See *The Rules of Distraction*, ADVOCATE (American Ins. Assoc.), Winter 2012, at 13, 15, available at <http://www.aiadc.org/AIAdotNET/docHandler.aspx?DocID=347498> ("Multitasking while driving, whether it be texting or talking on a cellphone or checking the directions on a GPS locator, is 'the most hazardous thing that a typical person does in a typical day,' says David Snyder, vice president and associate general counsel of the American Insurance Association."); see also Christina Bramlet, *Texting While Biking: Darwin Would Not Approve*, PROPERTY CASUALTY 360 (May 30, 2013), <http://www.propertycasualty360.com/2013/05/30/texting-while-biking-darwin-would-not-approve> ("[C]ompanies across the board, from insurers to automakers such as Volkswagen and Audi, to cell-phone providers—including AT&T, which recently created the #ItCanWait distracted driving campaign—are trumpeting safe driving practices via public awareness campaigns."). Insurers have supported laws both barring cellphone use altogether and requiring the use of hands-free devices for cell phone use while driving. See, e.g., *id.*

²⁴¹ See generally Omri Ben-Shahar & Kyle D. Logue, *Outsourcing Regulation: How Insurance Reduces Moral Hazard*, 111 MICH. L. REV. 197 (2012); see also 19 States Approve ISO's Telematics-Based Auto Rating Tool, INS. J. (Apr. 2, 2013), <http://www.insurancejournal.com/news/national/2013/04/02/286760.htm> (reflecting insurance industry's efforts to set premiums based on monitoring of policyholder driving behavior). I concede that, even in a regime of fragmented risk, insurers have an incentive to encourage risk-minimization as a means of reducing claims. For example, the Institute for Business & Home Safety receives substantial support and credit from insurers. See Remarks of Steven Weisbart, *supra* note 222; see also *New Swiss Re sigma study puts the spotlight on the role that insurance can play in improving food security for over 850 million people globally*, ENP NEWSWIRE (Jan. 18, 2013), <http://fpn.advisen.com/articles/article191877793->

Although recent scholarship suggests that insurers continue to play a risk-reducing, safety-enhancing role, it seems harder to find such dramatic examples of insurer-led safety advances today, at least in terms of tangible consumer products such as the UL-approved appliance, the seat belt, or the air bag. This may be the result of mere historical coincidence or misperception by observers. But it also may stem from the decrease in the comprehensive approach to insuring and perhaps from a decline in the industry's civic consciousness as well.²⁴²

To the extent that insurers can avoid risk through fragmentation and Swiss cheese approaches to underwriting and sales, they logically have a reduced incentive to seek to reduce risk in general. By contrast, where insurers provide coverage that is more comprehensive, they have more motivation to seek improvements that are more comprehensive in safety. When insurers provide broad coverage, they have an incentive to engage in broad efforts to reduce risk and loss. This in turn logically produces more public benefit than is produced by the efforts (or non-efforts) of insurers marketing more limited, fragmented insurance products.

This is not to say that insurers have lost all interest in improving safety. In addition to the modern examples cited above, auto insurers appear to be making substantial efforts to encourage safer driving by offering policyholders a discount in return for their willingness to be monitored and to drive safely

874756290.html (noting potentially useful role of agricultural insurance). Notwithstanding the fragmentation of property coverage, property insurers—particularly the large European reinsurers such as Munich Re and Swiss Re—have devoted significant study to problems posed by increasing levels of carbon in the atmosphere and attendant climate change. See Eduardo Porter, *For Insurers, No Doubts On Climate Change*, N.Y. TIMES, May 14, 2013, available at <http://www.nytimes.com/2013/05/15/business/insurers-stray-from-the-conservative-line-on-climate-change.html>.

²⁴² One arguable exception to this trend is that insurers have, to a degree, led the business community in noting the danger of climate change due to rising carbon levels in the atmosphere due to human activity. See Porter, *supra* note 241. However, insurers have largely tended to support adaptation efforts (e.g., stronger building codes, flood control projects) rather than mitigation efforts designed to reduce carbon emissions (e.g., a carbon tax, higher gas mileage standards, wind and solar power). See *id.*

(as verified by the insurer monitoring).²⁴³ However, in comparison to many insurance products, auto insurance remains largely a broad and comprehensive product despite some recent curtailments. The Swiss cheese aspects of contemporary homeowners policies and other insurance products may have drained some of the risk-reducing zeal from these insurers.

Supporters of fragmented coverage undoubtedly will respond that fragmenting risk does not necessarily relieve insurers as a whole from the risk. For example, a property policy may exclude pollution coverage, but, if environmental impairment insurance is sold to augment the now-reduced basic coverage, the environmental insurer retains substantial incentive to reduce risk through underwriting, monitoring, and other techniques. However, the market and risk pools for these more targeted and fragmented insurance products is thinner, resulting in policies that are less attractive to policyholders and, hence, less prevalent. A good deal of the impetus towards fragmenting risk appears not merely to direct the risk to insurers more adept at managing the risk, but to avoid the risk altogether unless the policyholder can pay high premiums.

To some degree, this makes economic and perhaps even ethical sense. No one is very excited about having the business community at large subsidize a subset of enterprises that pose substantial pollution or similarly difficult risks. But to the degree that these offenders fail to obtain insurance, or have only inadequate or very expensive insurance, the total social costs of this approach may be just as bad as the cross-subsidization that can take place through a comprehensive approach to insurance. With the relatively easy availability of bankruptcy and other debt avoidance techniques, the consequences of deadbeat polluters walking away and leaving taxpayers or victims with the

²⁴³ See Randall Stross, *So You're a Good Driver? Let's Go to the Monitor*, N.Y. TIMES, Nov. 24, 2012, available at <http://www.nytimes.com/2012/11/25/business/seeking-cheaper-insurance-drivers-accept-monitoring-devices.html>; Joseph B. White, *Auto Insurance Enters the 'Pay-per-View' Era*, WALL ST. J. (June 12, 2012, 7:01 PM), <http://online.wsj.com/article/SB10001424052702303901504577462382411135766.html>; see also Todd Wallack, *Privacy Is the Price for Lowering Car Insurance: Insurers Test Devices to Monitor Driving*, BOSTON GLOBE, Sept. 16, 2012, at A1 (examining insurers' efforts to monitor policyholders and encourage safe driving).

bill²⁴⁴ may be as or more negative than mandating broader coverage priced accordingly among a wider risk pool that includes many less risky entities.²⁴⁵

This counter-argument in favor of fragmentation may have some force in the commercial sector, where some entities regularly conduct riskier business than others and where many policyholders have the capacity to self-insure or otherwise craft apt risk management programs if not included in comprehensive policies. However, it seems far less persuasive when applied to the consumer context.

Consider the many limitations of some homeowners policies as discussed above, such as mold exclusions, the visible marks definition of theft, the criminal acts exclusion as applied to drunk driving, and the misconduct by “any” insured exclusion.²⁴⁶ In many or most of these instances, the policyholder is not involved in planned activity that creates the risk or loss. The

²⁴⁴ See LoPucki, *supra* note 229, at 78, 85.

²⁴⁵ I realize that Ken Abraham disagrees, at least implicitly, which of course gave me pause. See Abraham, *The Rise and Fall of Commercial Liability Insurance*, *supra* note 192 (noting that expansive coverage decisions by courts had the unintended consequences of prompting insurers to narrow coverage, particularly with the 1986 revisions to the CGL form, in effect resulting in reduced general liability protection for commercial entities going forward even though those expansive coverage decisions aided policyholders and victims regarding past problems with asbestos, pollution, and government-mandated waste clean-up). Applied to my proposed strengthening of the comprehensive approach, his analysis suggests that if forced to engage in comprehensive underwriting (by legislators, regulators, or courts), insurers will likely respond by exiting some markets or imposing lower policy limits and sufficiently high premiums, deductibles, or co-insurance requirements to make for a net welfare loss for policyholders and the public. Although I acknowledge this as a risk for commercial insurance, for the reasons set forth in text, I see it as not very threatening in the consumer context.

²⁴⁶ See *supra* TAN 137–98. Drug dealing spouses present a closer question. But it is often unrealistic to expect one insured to shut down another insured’s legal activity—and certainly unrealistic to expect the an insured aware of coverage-excluding activity to find the strength to stand in the way (perhaps at grave personal risk) in order to preserve insurance coverage. Optimism and self-serving biases make it likely that a co-insured will underestimate the risk of loss, and, if the co-insured is completely innocent by virtue of lack of awareness of a co-insured’s coverage-destroying activity, the exclusion or limitation creates no incentive for safety or precaution.

policyholder usually has had essentially no control over mold problems or the stealth and smoothness of the burglar who came to call—and certainly no control in most cases over the aberrant co-insured who goes insane or becomes unhinged over a divorce.²⁴⁷ Flood and earth movement exclusions to basic homeowners and other property coverage present the same situation, except to the extent that society is willing to embrace a position of “blaming” those who live near water or too near a fault line—and blame them enough to discourage insurance through the current Rube Goldberg system that denies comprehensive coverage in favor of ineffective fragmented underwriting.²⁴⁸

D. BENEFITS FOR INSURERS

In advocating for more inclusive insurance products, I confess to worrying primarily about unprotected policyholders and victims and the degree to which the costs of insurance failure are externalized upon society and government. But I am not insensitive to the interests of insurers, in particular their need to turn enough of a profit to offer the more inclusive policies sought.

The movement toward fragmenting coverage appears driven by factors of both ideology and business. Ideologically,

²⁴⁷ Some will argue that felony drunk driving is a different matter. Perhaps, but in many cases, an inebriated driver was simply someone who was insufficiently careful about alcohol intake (e.g., drinking strong cocktails instead of the usual wine or beer, drinking on an empty stomach, drinking on top of being tired at the end of the week) who then had the misfortune to be in a vehicular collision that caused serious injury or death. Although society should of course refrain from praising such errors in judgment and their consequences, treating these events as uncovered due to a new Puritanism merely deprives the victim of compensation and forgoes a sensible opportunity to spread the risk, particularly in the United States where automobile use is so widespread, and public transit and livery service are not always widely available.

²⁴⁸ To be sure, one can have a serious public policy debate about whether so much expensive property should be built so close to beaches, lakes, rivers, mountain tops, cliffs, edges, and the like (although this proximity is often a large part of what makes the property more expensive). Certainly, premiums should reflect the increased risk posed by such properties, but exempting such properties from risk distribution or creating a situation ripe for post-loss opportunistic behavior is not an apt response to the perceived problem.

advocates of fragmentation argue that policyholders ideally should pay only for the coverage they need rather than being forced into larger risk pools where they may be subsidizing riskier members of the pool and, hence, paying higher premiums than necessary.

Although this objection can seem well-taken, it stems from an erroneous, excessively sanguine view of the risk management capabilities of most policyholders. Although some individuals and commercial entities have a realistic view of the risks they face and make rationale calculations as to their risk management goals and insurance needs, this is hardly the norm. Policyholders, like all human beings, will often err in estimating their risk exposures and their insurance needs. Even the perfectly rational person or entity can simply miscalculate.²⁴⁹ Such is the nature of risk, at least if not dealing with a sufficiently large risk pool over a sufficiently large time. Add in the occasional unanticipated cataclysm, and the policyholder's estimate of what it "needs" for adequate protection can be very wrong.

Moreover, most policyholders are not perfectly rationale. Cognitive error abounds, both for individual humans and the humans who make risk management decisions for entities. They are afflicted by optimism bias, self-serving bias, short-term focus, and other heuristic errors²⁵⁰ that in turn will produce often-substantial miscalculations as to necessary insurance protection. Although these errors sometimes run in the direction of purchasing too much insurance,²⁵¹ more often, these

²⁴⁹ Regarding the types of common cognitive error exhibited by humans, see generally DANIEL KAHNEMAN, THINKING FAST AND SLOW (2011); SUNSTEIN & THALER, *supra* note 220; BEHAVIORAL LAW & ECONOMICS, *supra* note 220, at 1–10 (reviewing literature regarding cognitive traits, many of which often lead to reasoning errors such as constructed preferences, extremeness aversion, hindsight bias, optimistic bias, status quo bias, anchoring, the availability heuristic, loss aversion, and self-serving bias).

²⁵⁰ See JENNIFER K. ROBBENNOLT & JEAN R. STERNLIGHT, PSYCHOLOGY FOR LAWYERS 70, 71, 76, 77 (2012); BEHAVIORAL LAW & ECONOMICS, *supra* note 220, at 1–10; FARNSWORTH, *supra* note 220, at 21–26. See generally KAHNEMAN, *supra* note 249; SUNSTEIN & THALER, *supra* note 220.

²⁵¹ See Kent Syverud, *On the Demand for Liability Insurance*, 72 TEX. L. REV. 1629, 1647–49 (1994); Victor P. Goldberg, *The Devil Made Me Do It: The Corporate Purchase of Insurance*, 5 REV. L. & ECON. 1, 541–42 (2009).

cognitive deficiencies are likely to result in obtaining too little insurance relative to the risk and the policyholder's ability to bear it because of the general tendency toward optimism bias and the tendency to undervalue more distant dangers while focusing on immediate problems.

Further degrading the insurance calculations of many entities is the problem of defective agency and misaligned incentives. Entities purchase insurance through risk managers and brokers. These parties often are dominated by the short-term incentive to keep premiums (which are paid from current funds) as low as possible, even if this may come at the risk of larger costs incurred later, i.e. if the fragmented Swiss cheese policy does not cover claims or if the lower cost insurer quibbles over the claim.

A risk manager who saves funds now is more likely to get a raise, a bonus, a promotion, or job retention during a recession or time of corporate downsizing. Procuring more insurance or insurance from a more reputable carrier with a better claims-handling reputation is less likely to serve the risk manager's immediate career goals. When claims subsequently arise and the entity policyholder is confronted with no coverage or an insurer wrongfully disputing coverage, dragging its feet, or quibbling over valuation, the risk manager who was a hero a placement time may be one or two employers down the road.

The insurer brokerage house used by the policyholder has long-term interests in performing well and keeping business. But like the policyholder entity, it does its work through human agents who are often subject to the same short-term forces of self-interest that may cloud the broker's judgment and impair performance.

Policyholders may become dissatisfied with a broker and can always change brokers, but the competitive pool is limited. A handful or perhaps a dozen major brokers service nearly all the major commercial policyholders.²⁵² Although there are many

²⁵² See INS. INFO. INST., *THE INSURANCE FACT BOOK 2012*, 1, 4–6, 9–10, 12, 14–15, 20, 23 (2012), available at http://iiky.org/documents/Insurance_Factbook_2012.pdf; see also *Best's Review's Top Global Insurance Brokers*, BEST'S REVIEW (2012), available at [http://www.fci-benefits.com/fci/fci.nsf/0/10775CAAC76586F186257A4D00730C3A/\\$file/TopGlobalBrokers%202012.pdf](http://www.fci-benefits.com/fci/fci.nsf/0/10775CAAC76586F186257A4D00730C3A/$file/TopGlobalBrokers%202012.pdf); see also *The Reactions guide to insurance markets 2012*, REACTIONS (2012), available at <http://www.reactionsnet.com/pdf/2012Directory.pdf>; *Commercial*

regional and small brokers, they often cannot fully serve commercial policyholders. In turn, policyholders must work with wholesale brokers or the same dozen or fewer national/international firms with which the policyholder may be dissatisfied.²⁵³ Smaller brokers, even if authorized to fully handle a commercial account, are widely viewed by insurers and policyholders as having lower competence and expertise, making it unrealistic that a commercial policyholder can realistically do too much shopping for a new broker after losses start coming in, due to arguable oversight by a large broker now seen as having failed the policyholder.

Although policyholders may not gain from fragmented coverage, insurers currently appear to believe that they do—at least if the coverage is not so obviously fragmented as to discourage potential policyholders. Consequently, the Swiss cheese model can be economically attractive for carriers. Policies can be offered that look reasonably broad, but are riddled with coverage restrictions in the form of exclusions, sub-limits, narrow definitions, or demanding conditions. Less discerning brokers and risk managers—or discerning ones overcome by short-term financial considerations—will fail to realize the holes in coverage. Or they may be convinced that these coverage limitations are not holes but instead are ways of “tailoring” the policy (a favorite word of insurers not wanting to concede narrow coverage) to the needs of the policyholder in return for a lower premium.

Although I remain skeptical that this model is wise for any but the most knowledgeable policyholder freed of cognitive bias or agency concerns, I concede that it is probably a profitable mode of operation for the insurer. In return for some modest reduction in premium (which still leaves plenty of premium to invest), the insurer can excise entire categories of risk exposure.

Lines, INS. INFO. INST., available at http://www.iii.org/facts_statistics/commercial-lines.html#.UfvvK6n9CE8.email (last visited Nov. 22, 2013); *Insurance Company Rankings*, INS. INFO. INST., available at http://www.iii.org/facts_statistics/insurance-company-rankings.html (last visited Nov. 22, 2013).

²⁵³ Regarding the organization and delivery of insurance brokerage services, see generally BERTRAM HARNETT, RESPONSIBILITIES OF INSURANCE AGENTS AND BROKERS 2 (2013).

But my argument is not that fragmented risk is necessarily a bad deal for insurers. Rather, I contend that bundled or comprehensive risk can be an equally good or even better deal for insurers. For the same reasons articulated by Elmer Sawyer and his contemporaries at the dawn of the CGL form, bundling has both a marketing attractiveness and a pricing and investment attraction.²⁵⁴

The marketing advantage of the comprehensive policy is that it offers one-stop shopping to policyholders (at least for that particular risk), and it frees the policyholder and broker from much of the work of putting together a program of interlocking coverage, or determining whether the policyholder can forgo coverage in order to self-insure or simply “go bare” regarding the risk. To the extent insurers sell “peace of mind” and convenience as well as protection, there are some obvious advantages to the comprehensive policy that seem at least compatible with those offering tailored coverage marketed as being only what the policyholder “needs.”

As Sawyer and his contemporaries further noted, offering a bundle of comprehensive protection in turn permits the insurer to charge increased premiums.²⁵⁵ Although offering fragmented coverage to land is one business model, the more attractive model of offering more coverage in return for a higher premium seems advantageous. That is, so long as the policyholder is not paying for coverage far in excess of its needs, and the premium is not absolutely unaffordable. Then, the policyholder gets additional protection, convenience, and comfort, and the insurer, in return, receives increased funding for investment.

The importance of obtaining increased premiums cannot be overlooked. Berkshire Hathaway and its CEO, Warren Buffett, became wealthy largely due to the incoming premium dollars or “float” (Buffett’s seemingly preferred term) generated by comprehensive liability insurance. National Indemnity Co. and National Fire & Marine Ins. Co. (both purchased by Buffett in 1967) provided a substantial part of the cash used by the billionaire investor to burnish the bottom line of Berkshire Hathaway. Armed with accumulated premiums invested by

²⁵⁴ See TAN 38–57.

²⁵⁵ See TAN 36–40.

Buffett, Berkshire Hathaway and its insurers have done extraordinary well during the past four decades. Although other insurance executives may lack Buffett's fame and reputation, general liability and auto liability insurers offering relatively comprehensive coverage have also performed well during that time period, even though there have been more than a few years in which they shouldered combined ratios in excess of 100.²⁵⁶

Building premium receipts through offering more comprehensive coverage puts the insurer in a position similar to one who begins saving in youth. Even if the amounts are only a little bit larger, if left invested for many years the insurer will see something like the impact of the opening a Roth-IRA by a fifteen year-old. Even slight additional investments result in substantial wealth over time.

In addition, many of the insurer restrictions on coverage do not involve particularly problematic or grave risks. Insurers could include them in comprehensive coverage, even if not extracting a great deal more premium, and still face little increased risk exposure. These risks do not, even when aggregated, appear to present the types of problems that resulted in the asbestos and pollution exclusions. Insurers can absorb them, probably with no increase in premium and certainly with only a modest increase in premium.

For example, the burglary and theft coverage found in most property policies effectively requires (in the definitions section or another provision in the policy) that there be visible marks of forced entry in order to have coverage. Insurers have interposed this limitation on coverage with some success,²⁵⁷ but also some

²⁵⁶ See INSURANCE FACTS AND STATS, *supra* note 16, at 14–24; see also *Top 100 Groups Ranked By Net Premiums Written*, PROP. CASUALTY 360, *supra* note 16, at 34 (Berkshire Hathaway insurance operations had combined ratios below 100 in both 2011 and 2012); Kristin Jones, *Berkshire Hathaway's Earnings Climb 46%*, WALL ST. J., Aug. 2, 2013, <http://online.wsj.com/news/articles/SB10001424127887323997004578644412264377072>.

²⁵⁷ See, e.g., *Lumbard v. W. Fire Ins. Co.*, 381 N.W.2d 117 (Neb. 1986) (enforcing and rejecting public policy challenge to insurance policy definition of burglary that required visible marks of physical injury); see also *Cochran v. MFA Mut. Ins. Co.*, 271 N.W.2d 331 (Neb. 1978) (rejecting reasonable expectations challenge to enforcement of visible marks language).

well-known failures,²⁵⁸ as courts have on occasion involved the reasonable expectations concept to invalidate the restrictive language, reasoning that so long as the loss was not an inside job perpetrated by the policyholder, the visible marks requirement wrongly deprives the policyholder or coverage reasonably expected.²⁵⁹

Although this perhaps prompts the question of why insurers have not stayed with and expanded the comprehensive, Sawyer-esque model, my view is that the question is more likely answered by the intellectual Zeitgeist and cognitive error, rather than inexorable business forces. Although they were not fatal to the liability insurance industry, there is no doubt that asbestos, pollution, and Superfund claims put stress on the industry, prompting perhaps justified laser exclusions. In reaction, insurers became considerably more careful, perhaps even skittish about continuing the comprehensive approach. Once (or more often) burned, twice shy. This in turn activates the availability heuristic, the cognitive error that prompts people to think a risk is larger than it really is because they are now aware of it. Having witnessed the ravages of the asbestos mass tort, insurers are quicker to see (erroneously in my view) subsequent problems (e.g., mold) as presenting a similarly large—possibly even uninsurable—risk.

Meanwhile, a business Zeitgeist promoting fine-tuned customer products and consumer choice has become popular. In contrast to the spirit that animated the original CGL form,

²⁵⁸ See, e.g., *Atwater Creamery Co. v. W. Nat'l Mut. Ins. Co.*, 366 N.W.2d 271 (Minn. 1985) (recognizing clarity of policy text requiring visible marks of forced entry but ordering coverage based on objectively reasonable expectations of policyholder in light of hidden and surprising aspects of the visible marks exclusion, which was contained in a definition rather than a denominated exclusion); see also *C & J Fertilizer, Inc. v. Allied Mut. Ins. Co.*, 227 N.W.2d 169 (Iowa 1975) (same; also concluding that literal enforcement of visible marks language effectively made policy one failing of its implicit purpose).

²⁵⁹ To illustrate the weakness of the use of a visible marks requirement as a deterrent to inside jobs, consider theft by a savvy but unethical policyholder. Such a policyholder might simply load up a truck with valuables, even large quantities of inventory, intending to later claim that they were lost or stolen. If the hypothetical fraudulent policyholder wishes to enjoy the proceeds of the policy, he or she need merely break a window or kick in a door on the way out in order to have coverage.

which was one of trying to do the thinking for the policyholder and provide blanket coverage, the current ethos places more emphasis on selling coverage particular to the policyholder and attempting to interject more choice and potential premium savings. While this is laudable in the abstract, this modern conventional wisdom of insurance product design and marketing is at odds with similarly modern research on human perception, thinking, and choice—much of which frequently suggests that people are not good at making these decisions, and that they would be better served by being “forced” to accept more comprehensive products that did not permit them to error.

Insurers can profit by providing less fragmented, more inclusive coverage that eschews the Swiss cheese approach. The seventy-five years of experience with the CGL form attests to the ability of insurers to make money by bundling coverage and enjoying the marketing, pricing, and investment benefits of such products.

VI. OPERATIONALIZING THE MOVE TOWARD BROADER INSURANCE PRODUCTS: THE RESPECTIVE ROLES OF LEGISLATORS, REGULATORS, AND COURTS

A. THE INSUFFICIENCY OF IMPROVED TRANSPARENCY

As is now apparent, I lack the confidence many have in greater transparency and disclosure. Under this school of thought, mandated bundling of coverage is unnecessary. Rather, attention should be focused on providing prospective policyholders with more information about the coverage provided by various policies offered by various insurers.²⁶⁰

²⁶⁰ See generally Daniel Schwarcz, *Transparently Opaque: Understanding the Lack of Transparency in Insurance Consumer Protection*, 61 U.C.L.A. L. REV. (forthcoming 2014); see also Schwarcz, *Reevaluating Standardized Policies*, *supra* note 10, at 1337–40 (also suggesting mandated minimum coverage and greater use of default rules or provisions providing adequate protection to policyholders). Transparency often is a politically attractive solution to a perceived consumer protection problem because it provides at least theoretical benefits to consumers without imposing direct regulation on vendors. See, e.g., *N.J. Law Requires Insurers to Provide 1-Page Summary of Homeowners Coverage*, INS. J. (May 7, 2013), <http://www.>

When presented with an adequate opportunity to comparison shop, policyholders will gravitate toward purchasing broader with fewer gaps, either by opting for policies that bundle or by themselves purchasing the necessary array of policies.

Although a world with more transparency and available information is generally better than one with less, disclosure alone will not fix the problem of excessively fragmented risk. In some cases, expanded information may only confuse consumers.²⁶¹ Consider the privacy notices mandated by HIPAA and the package inserts found in prescription and over-the-counter medicines. They go unread, or, if read, may only induce decision paralysis or prompt incorrect decisions (e.g., spurning use of a helpful drug because the package insert mentions a rare side effect about which the patient is abnormally skittish).²⁶²

A substantial body of cognitive research, much of it addressed by contract scholars, makes a powerful case

insurancejournal.com/news/east/2013/05/07/291128.htm (law requires “clearer” explanations by insurer according to co-sponsor but does not require policies to be available on line and does not establish minimum coverage requirements).

²⁶¹ See Russell Korobkin, *Bounded Rationality, Standard Form Contracts, and Unconscionability*, 70 U. CHI. L. REV. 1203, 1272 & n.271 (2003); see also *Fisher v. Ford Motor Co.*, 224 F.3d 570, 574 (6th Cir. 2000) (“NHTSA feared ‘information overload,’ i.e., that additional warnings would distract from the warnings it had determined were critical, leading consumers not to focus properly on the latter. It was also concerned that additional warnings might simply lead people to pay no attention to any of them.” (citation omitted)); Melvin Aron Eisenberg, *Text Anxiety*, 59 S. CAL. L. REV. 305, 305 (1986) (“My thesis is that consumers who are faced with the dense text of form contracts characteristically respond by refusing to read, and that it is reasonable for them to do so.”).

²⁶² See Nathan Cortez, *Do Graphic Tobacco Warnings Violate the First Amendment?*, 64 HASTINGS L.J. 1467, 1497–98 (2013) (“Textual consumer product warnings are becoming more and more stale and ineffective. First, they are probably overused. As Lars Noah observed almost twenty years ago, the ‘proliferation of warnings may dilute the impact of truly important cautionary information.’ The FDA, in fact, has long recognized the need to resist diluting its warnings and overloading consumers with information. Other agencies have recognized the problem too. Media often mock our propensity to overwarn.” (footnotes omitted)). See generally Lars Noah, *The Imperative to Warn: Disentangling the “Right to Know” from the “Need to Know” about Consumer Product Hazards*, 11 YALE J. ON REG. 293 (1994).

suggesting that disclosure simply is not very effective and that prohibition of unfair contract terms or promotion of useful terms holds substantially greater promise for improving consumer welfare.²⁶³ Based on this research and analysis, it seems certain that disclosure alone is insufficient. Although greater information and transparency have an important role to play in improving insurance markets, the case for inclusive insurance is probably best made through mandated coverage and limiting undue restrictions on coverage.

Transparency might be helpful, however, not so much for facilitating consumer understanding of policy terms, but for apprising consumers of insurer track records regarding coverage, claims processing, payment, and customer satisfaction.²⁶⁴ Although the tendency toward cognitive error

²⁶³ See Omri Ben-Shahar & Carl E. Schneider, *The Failure of Mandated Disclosure*, 159 U. PA. L. REV. 647, 666 (2011) (“There is much evidence that consumers do not read [Truth in Lending Act of 1968] disclosures, are overloaded by the number of disclosures, and do not understand the basic disclosed features of the loan.”); see also Cortez, *supra* note 262, at 1498 (“[M]any widely accepted disclosure requirements are demonstrated to be ineffective. For example, many physicians disregard the warnings in pharmaceutical labels, even so-called ‘black box’ warnings required for the most severe risks. In fact, the FDA has ‘openly chastised physicians for disregarding instructions in the labeling for newly approved drugs,’ and has turned to more aggressive mechanisms like requiring risk management plans. Likewise, in 2007, the Institute of Medicine concluded that cigarette warnings, last updated in 1984, had become stale and ineffective.” (footnotes omitted)); Omri Ben-Shahar, *Fixing Unfair Contracts*, 63 STAN. L. REV. 869 (2011) (noting the prevalence of unfair contract terms and arguing that law should impose minimally fair or “tolerable” terms for consumers); Oren Bar-Gill & Kevin Davis, *Empty Promises*, 84 SO. CAL. L. REV. 1, 1–2 (2010) (vendor contractual promises of decreasing utility to consumers because vendors reserve right of unilateral modification; consumers fail to adequately appreciate the risks posed and potential injury; legal system provides insufficient protection for consumers in such situations); Oren Bar-Gill, *The Behavioral Economics of Consumer Contracts*, 92 MINN. L. REV. 749, 749 (2008) (noting degree of consumer cognitive error and concluding greater legal protection of consumers is desirable). See generally Oren Bar-Gill, *Bundling and Consumer Misperception*, 73 U. CHI. L. REV. 33 (2006) (consumers may have cognitive limits on ability to evaluate products and services and are often unable to determine whether bundling or unbundling of such products and services is in their best interests).

²⁶⁴ See Schwarcz, *Transparently Opaque*, *supra* note 260 (discussing the benefits of disclosure, particularly, its ability to facilitate comparison-shopping

and short-term maximization²⁶⁵ may yet prompt policyholders to foolishly choose the cheapest insurer even if it has a horrible track record in paying claims, there is at least a fighting chance that if insurer performance information and consumer complaint information is more widely available that it will influence purchasing decisions.

B. LEADING WITH SENSIBLE REGULATION

Ideally, most of the impetus for change would come from regulators. Despite concerns over industry capture of insurance regulators, administrative solutions would be most effective. Regulators could require that basic insurance policies include the breadth of coverage necessary to provide what experts regard as essential protection in particular lines of insurance. In doing so, regulators could police the policy language to ensure that what is provided in the “large print” of the insuring agreement is not taken away by the “small print” of unknown or difficult to decipher exclusions, conditions, and definitions.²⁶⁶ Although policies could of course be customized to accommodate policyholder needs and requests through endorsements and riders, these would also be subject to insurance department scrutiny.

In particular, state regulators should require that property policies, particularly those sold to consumers, include coverage for the major external perils, i.e. risks such as water damage, flood, and earthquake which historically have been thought too difficult for private insurers to bear. But as part of this process,

and result in greater market discipline for insurers); *see also* Schwarcz, *Re-evaluating Standardized Policies*, *supra* note 10, at 1337–40; Ed Beeson, *Demystifying insurance: put policies online for anyone to see*, *Rutgers professor says*, THE STAR-LEDGER, Feb. 10, 2013, http://www.nj.com/business/index.ssf/2013/02/demystifying_insurance_put_pol.html (discussing Jay Feinman’s views on access to insurance policies).

²⁶⁵ *See* TAN 256–259 regarding cognitive error and short-term maximization distorting individual judgment and entity insurance decisions.

²⁶⁶ State insurance regulators generally have substantial power, even if it not always well deployed. *See* STEMPEL ET AL., *supra* note 16, at ch. 3. Because of longstanding national custom largely codified in the McCarran Ferguson Act, 15 U.S.C. §§ 1011–1015, the locus of insurance regulation is state-centered. *Id.*

regulators must permit carriers to charge an adequate premium and at least do nothing to retard insurer pursuit of adequate capital and reinsurance.

Part of the regulatory effort must also work to ensure that all similarly situated insurers compete on a level playing field, so that some are not allowed to gain customers by providing inadequate but less expensive coverage. If, for example, all homeowners' insurers are required to provide flood and earthquake coverage, all will have to price accordingly. No insurer should get punished for "doing the right thing" in offering inclusive coverage. Nor should insurers be required to offer more comprehensive coverage at a loss because regulators will not approve adequate premium rates.

Regulation in this area needs to be improved so that policy provisions and differential treatment of risk is adequately supervised, with insurers required to justify disparate treatment of risks. If state insurance departments fail to adequately shoulder this task, as discussed below, courts should be willing to apply a stronger version of contract doctrines such as reasonable expectations, estoppel, reformation, unconscionability, and public policy to prevent insurers from imposing unreasonably favorable or excessively risk-fragmenting terms on policyholders.

Conversely, regulators must be willing to let genuine market forces set prices and permit insurers to price bundle coverage in a manner that ensures their effectiveness and industry solvency. A long-running problem of insurance regulation is that it tends to be toothless, often completely failing to provide policyholders with sufficient information to make informed choices, and it typically lacks any real effort to police oppressive contract terms or to improve the insurance placement process.²⁶⁷ For example, many—if not most—policyholders are unable to even see the insurance policy they purchased until it arrives in the mail weeks or even months later.²⁶⁸ When regulators become

²⁶⁷ See Schwarcz, *Transparently Opaque*, *supra* note 260.

²⁶⁸ See *id.* (policy delivery usually two to three weeks after purchase). This is also an issue in commercial insurance. For example, the lessee of the World Trade Center assumed control of the property on July 1, 2001 and was insured pursuant to oral agreements and an short written binder – but the actual written policies had not yet been issued at the time of the September 11 terrorist

invigorated to regulate something beyond carrier solvency, their core concern,²⁶⁹ it is usually to seek public approval in advocating to keep lower premiums, something more likely to happen if the state insurance commissioner is positioning to run for higher office.²⁷⁰

But regulation that seeks or obtains artificially low premiums only hurts the cause of intelligent risk management and affordable insurance—at least if one counts all of the costs. If insurers are denied the ability to charge an adequate premium, they can engage in destructive behavior even if not moved to exit the state or to cease offering the insurance product at issue. Consider a hypothetical insurer seeking a 20% rate increase in a Gulf Coast state due to heavy hurricane losses the previous year. The insurance commissioner, with the senatorial primary only weeks away, makes a big splash in the press by approving only a

attack on the buildings. See Jeffrey W. Stempel, *The Insurance Aftermath of September 11: Myriad Claims, Multiple Lines, Arguments over Occurrence Counting, War Risk Exclusions, the Future of Terrorism Coverage, and New Issues of Government Role*, 37 Tort & Ins. L.J. 817, 833-34 (2002). See also *id.* at 833, n.64 (time lags of this sort between purchase of insurance and production of written policy itself are not unusual. See also Schwarcz, *Reevaluating Standardized Policies*, *supra* note 10, at 1319-28 (criticizing insurance regulator failure to require that policy forms be available for inspection by prospective policyholder prior to purchase and finding other sources of information inadequate substitutes for regular-forced increased transparency); Beeson, *supra* note 264 (discussing lack of consumer access to fine print of their policy).

²⁶⁹ See KENNETH S. ABRAHAM, *INSURANCE LAW AND REGULATION: CASES AND MATERIALS* 122 (5th ed. 2010).

²⁷⁰ See Kunreuther & Pauly, *Insurance: The Most Misunderstood Industry*, *supra* note 82 (“State regulators often constrain insurance premiums because they are concerned that insurance will not be ‘affordable,’ especially to those who are at higher risk Behavior of this kind defeats the three principal purposes of insurance: to provide information via premiums as to how serious your risk is; to provide motivation for undertaking financial protection against an event that could produce a significant loss but has a low probability of occurrence; and to offer incentives in the form of premium reductions to reward people who invest in risk-reducing measures.”); see also STEMPER ET AL., *supra* note 16, at ch. 3. See generally NAT’L ASSOC’N OF INS. COMM’RS, *STATE INSURANCE REGULATION* 3 (2011), available at http://www.naic.org/documents/topics_white_paper_hist_ins_reg.pdf (“regulators may seek to ensure that policy benefits are commensurate with the premiums charged”).

5% increase. The rational insurer (assuming it was also an ethical insurer that really needed a 20% increase and was not just posturing) will, if it stays in business in the state, react by being tougher on claims and paying them more slowly. When it has a chance to revise its standard policies, it will restrict coverage if possible or use revised policy language more favorable to disputing, reducing, or denying claims.

In the end, the consumer may be much worse off than if the insurer had been permitted the 20% premium increase sought.²⁷¹ Put another way, which situation would the average person prefer: paying one-fifth more in premiums and being promptly covered via a fair claims process in the event of a loss; paying only 5% more in premiums but having to wait for claims payment; accepting a lowball offer (but not so lowball as to make litigation worthwhile); or having a borderline or mixed claim denied rather than receiving the benefit of the doubt from the insurer? Although policyholders might at first favor lower premiums and short-term interest, most would, upon reflection, probably rather have longer-term protection and not claim hassles. “You get what you pay for” may be a cliché, but it has become so because of its general accuracy.

Although homeowners’ insurance and its typical lack of flood or earthquake coverage provides perhaps the best example of fragmented risk coverage that needs change, nearly every insurance product can provide more comprehensive coverage, provided that all insurers are required to offer a minimum of coverage and are permitted to charge apt premiums for the coverage. In this way, regulators can prevent Swiss cheese policies or insurers from unfairly stealing market share from insurers and products that provide the protection consumers expect or need.²⁷² Under the current regime, insurers are able to

²⁷¹ In the interests of equilibrium, regulators should also be willing to demand rollbacks in premiums if conditions change in favor of insurers and the market is insufficiently competitive to create momentum for reduced prices. Generally, however, it appears that insurance pricing does respond to soft market conditions, making it likely that the insurers who increased premiums 20% in Year 1 will be required to reduced premiums in Year 4 in response to market conditions that resulted in their competitors offering lower prices.

²⁷² Although objectively reasonable policyholder expectations are not a bad yardstick for determining the proper amount of coverage that should be available in a type of policy (e.g., homeowners expect coverage if mold

offer products that policyholders incorrectly perceive as broader than they are, and to price Swiss cheese insurance as though it were comprehensive coverage. Insurers have incentives to offer increasingly limited coverage under the guise of broad coverage and can easily fool most policyholders most of the time, including the sophisticated ones. Under these circumstances, the market is inadequate to the task of providing sounder risk management unless regulators insist on adequately comprehensive coverage.

Even insurers receptive to mandated coverage for flood will argue that this requires government-backed reinsurance to permit them to accept the risk of widespread losses with the potential for clustered damages. Insurers taking this position implicitly suggest that risks such as flood and earthquake are akin to war and nuclear incident in that they are too great to be shouldered by the insurance industry alone.

I remain skeptical and continue to think that if all policies must provide coverage, and the market for coverage is robust, that bundled coverage can be accomplished through adequate pricing by insurers (assuming that regulators will not stand in the way of proper risk-based pricing). For homeowners' insurance, the private sector logically should need little assistance. Most homes are purchased with mortgages, and lending banks require insurance, creating a steady demand. Homeowners will not be allowed to forgo insurance and will be forced to buy the more comprehensive products including flood, earthquake, and perhaps additional coverage. This may be paternalism or even a "nanny state" approach, but it sure appears more attractive than the status quo. In addition, reinsurance should be widely available in the private sector, particularly if insurers are pricing the product at levels attractive to quota share reinsurance.²⁷³

spreading through their drywall causes property damage or makes the dwelling uninhabitable), it is not the only yardstick. Consumers and less sophisticated commercial policyholders often simply lack enough knowledge of risk to know what coverage should be available in a basic policy. Insurers and regulators often have that knowledge and, consequently, should bring it to bear in crafting the amount of minimally comprehensive coverage that insurers must offer.

²⁷³ Reinsurance is often written on a "treaty" basis with the ceding company (the insurer wishing to obtain reinsurance on the risk ceded to the reinsurer), which is essentially a reinsurance agreement as to an entire book of business

If the insurance industry is not able to take on flood or certain other big risks without government reinsurance, government-reinsured flood and earthquake coverage may be a necessary government supplement to the private insurance market. By analogy, life insurance proved impossible for active duty soldiers to purchase, requiring the U.S. government to at least subsidize such programs.²⁷⁴ Notwithstanding some problems with the operation of those programs by the insurers with whom the government works,²⁷⁵ this was a positive

held by the ceding insurer. This is contrasted with facultative reinsurance that is a contract designed to cover a narrower and more specific risk (although it may involve many policies and many million dollars. The reinsurance agreement itself may be a “quota share” agreement, in which the insurer gives up a portion of its premiums in return for the reinsurer’s commitment to share in an equivalent portion of any losses incurred under the policy or group of policies. By contrast, an excess of loss reinsurance agreement involves the insurer’s payment of a premium in return for the reinsurer’s commitment to provide coverage if the insurer’s losses on the risk exceed a specified triggering or attachment point. See STEMPER ET AL., *supra* note 16, at 1180–85; see also JERRY & RICHMOND, *supra* note 18 at ch. 14; STEMPER ON INSURANCE CONTRACTS, *supra* note 18, at §17.01; Patrick L. Brockett, Robert C. Witt & Paul R. Aird, *An Overview of Reinsurance and the Reinsurance Markets*, 9 J. INS. REG. 432 (1991) (outlining the types of reinsurance). See generally BARRY R. OSTRAGER & MARY KAY VYSKOCIL, *MODERN REINSURANCE LAW AND PRACTICE* (2d ed., 2000) (discussing quota share and excess of loss).

²⁷⁴ Servicemember’s Life Insurance is life insurance made available to U.S. Military personnel who would otherwise be able to obtain only life insurance containing a war exclusion, which, of course, would be of limited utility to active duty military personnel (but would nonetheless have some utility as servicemen can die of disease, auto accidents, or other causes that are not sufficiently war-related to be subject to the exclusion). These life insurance policies are offered by a private insurer under contract with the U.S. government, with the government agreeing to provide funds if the program suffers more losses than revenue. See Emmet J. Vaughan & Therese Vaughan, *Fundamentals of Risk and Insurance* 239-40 (8th ed. 1999); Patrick M. Callan, et al., *Analysis of Servicemembers’ Group Life Insurance (SGLI) Program: History, Current Issues and Future Implications* (MBA Thesis, Naval Postgraduate School, June 2011) at p. 9–10.

²⁷⁵ See David Evans, *Fallen Soldiers’ Families Denied Cash as Insurers Profit*, BLOOMBERG (July 28, 2010, 7:00 AM), <http://www.bloomberg.com/news/2010-07-28/fallen-soldiers-families-denied-cash-payout-as-life-insurers-boost-profit.html>; see also David Evans, *New York Said to Require Payments After Fallen Soldier Story*, BLOOMBERG (Feb. 23, 2012, 3:14 PM), <http://www.bloomberg.com/news/2012-02-23/new-york-said-to-require-life->

development for military personnel and their families. If an analogous effort is required to make flood and earth movement coverage part of the basic homeowners' policy or business owners' property policy, government should take on the task.

Legislators logically have less of a role unless regulators prove inadequate to the task. Most states already have extensive insurance codifications that will not require much modification to spur the cause of comprehensive coverage, except to the extent that regulators may need more express power to mandate certain coverage, bar certain restrictions, and police policy provisions. To the extent that insurers backslide on their commitments during the claims process, states may need to pass stronger bad faith laws with greater penalties or enlarge the successful claimant's right to payment of counsel fees by insurers.²⁷⁶

Executives other than those in the relevant insurance regulatory administrative agency also would presumably have less of a role beyond that of appointing competent insurance commissioners and judges, particularly judges with a more functionalist or instrumentalist approach to insurance coverage.²⁷⁷

insurer-payments-after-fallen-soldier-report.html; Matthew Sturdevant, *Life Insurance Practice Under Fire: Retained-Asset Accounts Draw Scrutiny From Veterans Affairs and New York's AG*, HARTFORD COURANT (Conn.), Aug. 2, 2010, http://articles.courant.com/2010-08-02/business/hc-life-insurance-controversy-20100802_1_retained-asset-accounts-insurance-prudential-financial/2.

²⁷⁶ See generally FEINMAN, *supra* note 12, at 202–22.

²⁷⁷ Judicial formalism tends to look for set rules that are then enforced as literally as feasible. In insurance matters, it often employs textualism, which is the view that contract disputes should if possible be decided according to the text of the insurance policy or other contract documents if the text is sufficiently clear. See STEMPER ET AL., *supra* note 16, at § 2.03. This approach is slow to concede linguistic ambiguity and tends to resist consideration of the reasonable expectations of the policyholder, considerations of public policy, and the implications of the product-like status and social instrument functions of insurance. By contrast, functionalist or instrumentalist approaches to insurance are receptive to consideration of these other factors and are more willing to see sufficient textual ambiguity to consider extrinsic evidence and are also less willing to read policy text literally. See *id.* at ch. 2.

C. THE ROLE OF COURTS

In restricting fragmented insurance to its proper scope, courts also have a role to play, particularly to the extent that legislators, regulators, governors, and the insurance industry do not take sufficient action. As compared to current jurisprudence, the role of courts will likely be more expansive in that courts are often directly faced with problematic insurance policy provisions or claims-processing behavior. After something of an apogee of functionalist contract construction culminating in the *Second Restatement*,²⁷⁸ most modern contract decisions have taken a more formalist, textualist tone overall,²⁷⁹ which, as a practical matter, has been favorable to insurers seeking to restrict coverage or create Swiss cheese coverage.²⁸⁰

Insurance law's healthy regard for the *contra proferentem* principle of construing ambiguities against the drafter and of appreciating the reasonable expectations of the insured have

²⁷⁸ See RESTATEMENT (SECOND) OF CONTRACTS (1981).

²⁷⁹ See Peter N. Swisher, *Judicial Rationales in Insurance Law: Dusting Off the Formal for the Function*, 52 OHIO ST. L.J. 1037, 1047 (1991) ("Legal Formalism continues to exist as a viable rationale for judicial decisionmaking in insurance law, which is largely based upon a traditional contractual interpretation of insurance policies generally."); see also Edward L. Rubin, *The Nonjudicial Life of Contract: Beyond the Shadow of the Law*, 90 NW. U. L. REV. 107, 107 (1995). G. Richard Shell, *Contracts in the Modern Supreme Court*, 81 CAL. L. REV. 433, 495-96 (1993).

²⁸⁰ See Peter N. Swisher, *Judicial Interpretations of Insurance Contract Disputes: Toward A Realistic Middle Ground Approach*, 57 OHIO ST. L.J. 543, 579-85 (1996). To the extent a court is more formalist, textualist, and literal in its approach, this tends to advantage insurers. Insurers normally are the final if not the sole authors of policy text and can often add coverage limiting language to standard forms or predecessor forms at will, limited by market conditions and policyholder sophistication and resources. Thus, for Swiss cheese policies such as some of the homeowners' policies discussed in Schwarcz, *Reevaluating Standardized Insurance Policies*, *supra* note 10, at 1277-1303, a formalist court is likely to enforce coverage-limiting language in the insurers favor, while a functionalist court is more likely to interpret the policy adverse to the policyholder through methods of interpretation beyond the text. See STEMPEL ET AL., *supra* note 16, at § 2.03.

mutated formalism to some extent,²⁸¹ but there is no shortage of insurance coverage cases taking an over-literal approach to text (decisions giving broad application to the CGL pollution exclusion²⁸² are a good example) or misunderstanding the nature of insurance when applying policy provisions.²⁸³ An approach to insurance policy construction more sensitive to the non-contract traits of insurance policies²⁸⁴ and the role of insurance on modern society²⁸⁵ can improve judicial analysis and case outcomes.

In addition, courts can advance the cause of more inclusive insuring through greater use of concepts such as unconscionability and public policy. Both of these concepts can be used to reform or strike down policy provisions that, if read and enforced literally, would do too much damage to the anti-fragmentation project as well as to the reasonable expectations of policyholders. A recent federal district court case provides an example of a useful judicial approach to limiting language in a policy.

²⁸¹ See Swisher, *Judicial Interpretations*, *supra* note 280, at 586; see also ROBERT H. JERRY, II & DOUGLAS R. RICHMOND, UNDERSTANDING INSURANCE LAW §§ 25A-F (5th ed. 2012) (discussing insurance contract interpretation and describing insurance version of contract law that tend to favor policyholders); STEMPEL ON INSURANCE CONTRACTS, *supra* note 3, at §§ 4.08–4.14 (same); ANDERSON ET AL., *supra* note 3, at §§ 2.01–2.09 (same).

²⁸² See generally Stempel, *Reason and Pollution*, *supra* note 95 (reviewing background and application of the pollution exclusion); Jeffrey W. Stempel, *Unreason in Action: A Case Study of the Wrong Approach to Construing the Liability Insurance Pollution Exclusion*, 50 FLA. L. REV. 463 (1998) (examining particularly bad decisions of Florida Supreme Court in this regard).

²⁸³ See, e.g., *Minnesota Fire & Casualty Co. v. Greenfield*, 855 A.2d 854 (Pa. 2004); see also STEMPEL ET AL., *supra* note 16, at 74–76 (criticizing *Greenfield* and noting that the impact of the decision merely deprives drug overdose victim's family of source of compensation).

²⁸⁴ See Jeffrey W. Stempel, *The Insurance Policy as Thing*, 44 TORT TRIAL & INS. PRAC. L.J. 813 (2009); see also Daniel Schwarcz, *A Products Liability Theory for the Judicial Regulation of Insurance Policies*, 48 WM. & MARY L. REV. 1389 (2007). See generally Jeffrey W. Stempel, *The Insurance Policy as Statute*, 41 MCGEORGE L. REV. 203 (2010).

²⁸⁵ See generally Jeffrey W. Stempel, *The Insurance Policy as Social Instrument and Social Institution*, 51 WM. & MARY L. REV. 1489 (2010).

In *Philadelphia Indemnity Insurance Co. v. Chicago Title Insurance Co.*,²⁸⁶ the court provided an example of the type of judicially enforced broader coverage in the face of policy language to the contrary, in effect, mandating a minimum degree of coverage. The court required the insurer to provide the policyholder/defendant with a complete defense to the entire action rather than fragmenting the duty to defend and restricting it only to certain claims against the policyholder/defendant.²⁸⁷ The case involved a series of complex commercial controversies, but the insurance question was relatively simple: did a primary insurer have a duty to defend the entire *case* against a policyholder, or could it rely on quite clear language that stated the insurer was required *only* to defend potentially covered claims?²⁸⁸ An excess insurer, anxious not to be required to defend when coverage pursuant to the underlying primary policy had been triggered, challenged the primary carrier's limitation.²⁸⁹ The primary policy contained fairly clear language that seemingly limited the insurer's duty to defend to only the "claims" that were potentially covered, rather than to the entire lawsuit, which is the standard insurance industry approach to the duty to defend.²⁹⁰

²⁸⁶ 871 F. Supp. 2d 744 (N.D. Ill. 2012).

²⁸⁷ *Id.* at 756.

²⁸⁸ *Id.* at 751–56.

²⁸⁹ *Id.* at 747.

²⁹⁰ *Id.* at 748. Specifically, the provision in question stated:

Upon written request by the insured, . . . [Chicago Title], at its own cost and without unreasonable delay, shall provide for the defense of an insured in litigation in which any third party asserts a claim adverse to the title or interest as insured, but only as to those stated causes of action alleging a defect, lien or encumbrance or other matter insured against by this policy. [Chicago Title] shall have the right to select counsel of its choice (subject to the right of the insured to object for reasonable cause) to represent the insured as to those stated causes of action and shall not be liable for and will not pay the fees of any other counsel. [Chicago Title] will not pay any fees, costs or expenses incurred by the

After initially denying the excess carrier's motion for judgment on the pleadings, the court granted summary judgment to the excess insurer on the issue based on "the well-settled Illinois rule" that an insurer required to defend any claim against the policyholder was obligated to defend "all counts in the lawsuit."²⁹¹ The court found—as a matter of law—that the limiting language of the primary policy was ineffective to narrow the insurer's duty to defend because the duty was indivisible as a matter of law.²⁹² In so ruling, the court rejected the primary insurer's argument that the duty to defend the entire case was only a default rule that could be contracted around by the parties through the policyholder's purchase of a policy providing for defense of only covered claim.

Although it might have found other grounds for refusing to enforce the limiting language of the Chicago Title policy,²⁹³ the court prevented enforcement of the limiting language more forcefully by effectively holding that a liability policy with a duty to defend feature was not legitimate unless it defended the entire action against the policyholder. Despite its earlier denial of the excess insurer's judgment on the pleadings motion and accompanying statements supportive of the primary insurer, the court, "[u]pon further research and careful consideration of the parties' arguments . . . conclude[d]" that Chicago Title could not

insured in the defense of those causes of action which allege matters not insured against by this policy.

Id.

²⁹¹ *Id.* at 751 (quoting *Pekin Ins. Co. v. Wilson*, 930 N.E.2d 1011, 1015 n.2 (Ill. 2010)).

²⁹² *Chicago Title*, 871 F. Supp. 2d at 751–53.

²⁹³ For example, the court could have determined that it would be unfair to apply the language against the policyholder due to the fact that the policy arriving weeks after placement and was probably unread when it arrived, or because the language was deceptive or hidden. See *supra* TAN 266-70 (describing such factors as a basis for the reasonable expectations approach to insurance policy construction and noting its application in cases refusing to enforce clear language requiring "visible marks" for forced entry for burglary coverage with this limitation contained in a policy definition rather than a policy exclusion).

legally contract around the complete defense rule” mandated by Illinois law.²⁹⁴

While the precedent upon which the court relied is arguably not as compelling as it suggested, *Chicago Title* is absolutely correct in refusing to allow the insurer to avoid the obligation to provide a total defense when one considers the overall structure of liability insurance, the purpose and function of liability policies, and the role played by liability policies in commercial risk management and the overall economy. If the primary insurer’s language had been given effect, the policy at issue would be a defective insurance product that should not be permitted—both because it defeats the objectively reasonable expectations of most policyholders and because it fails its essential purpose of providing efficient “litigation insurance.”

As cases like *Chicago Title* reflect, even a policy with clear text may be unworthy of enforcement by courts. Although insurance will always be primarily a subset of basic contract law, courts must do more than merely scrutinize text not only to provide better adjudication generally,²⁹⁵ but also to minimize the modern trend toward risk fragmentation. Courts should decide coverage cases with sufficient regard for what might be deemed an “anti-fragmentation principle.” Cases like *Chicago Title* may be viewed by some as undue judicial activism, but judicial willingness to depart from a more circumscribed role of merely reading policy language without thought about policy impact, function, and party intent and expectations can be an important part of resisting insurer efforts to manufacture Swiss cheese policies plagued by coverage gaps.²⁹⁶

²⁹⁴ *Chicago Title*, 871 F. Supp. 2d at 752.

²⁹⁵ See DAVID G. EPSTEIN, BRUCE A. MARKELL & LAWRENCE PONOROFF, CASES AND MATERIALS ON CONTRACTS: MAKING AND DOING DEALS 1 (3d ed. 2011) (the “contract” between the parties is their agreement or understanding, not the piece of paper on which that agreement is memorialized).

²⁹⁶ For additional recent examples of courts sensibly rejecting insurer attempts to avoid coverage (or, more specifically, the duty to defend) notwithstanding arguably favorable policy language, see, e.g., *Greystone Construction, Inc. v. National Fire & Marine Insurance Co.*, 661 F.3d 1272 (10th Cir. 2011) (general liability insurer must defend construction defect suit against policyholder notwithstanding insurer’s company-specific exclusions purporting to narrow coverage beyond exclusionary language in standard CGL policy); *Newman v. Scottsdale Insurance Co.*, 301 P.3d 348 (Mont. 2013)

D. THE NEED FOR LEADERSHIP BY AN INDUSTRY WITH ENLIGHTENED SELF-INTEREST

Although fragmenting risk can be an effective business model or technique for improving profits, the story of Sawyer and the CGL form, as well as other broad based insurance products such as auto insurance and homeowners' insurance (at least prior to the recent advent of departure from standardization and gaps in coverage), shows that comprehensively written products can support a profitable insurance industry. Bundled, comprehensive products will be more attractive to many consumers, particularly those less sophisticated consumers with fewer risk management resources. These consumers will prefer broader protection to the potential opportunity to save some premium dollars and the attendant additional risks this entails. This should facilitate more efficient and improved marketing by insurers, as well as streamlined policy issuance. Underwriting may at first be more difficult with more comprehensive products, but, ultimately, the actuarial calculation of risk should be as easy for bundled products as for fragmented products. Bundled, comprehensive products will therefore command a higher premium, better supporting the insurer's ability to profit from playing the float on premium dollars used for investment.

Some insurers may contend that they could earn more money over the long haul by selling fragmented coverage rather than bundled coverage. However, it seems unlikely that whatever loss ratio gains may come from insurer's narrower targeting of risk will be much greater than the marketing, premium sales, and investment gains more likely to be had under a more comprehensive approach. In either event, insurers are likely to be significantly more profitable than most companies in most other industries.²⁹⁷ So long as the profit

(insurer must defend parents' claim arising out of girl's death while at "tough love" academic boot camp). See also Michael Buck, *Fla. Court Rules Insurer Cannot Limit Sinkhole Coverage*, BEST'S NEWS SERVICE (Mar. 15, 2013), <http://www.programbusiness.com/news/Florida-Court-Rules-Insurer-Cannot-Limit-Sinkhole-Coverage> (court enforces state insurance department regulation barring exclusion of sinkhole coverage).

²⁹⁷ Although some (e.g., Dr. Weisbart; *supra* note 222, argue that insurance companies are not all that profitable (or at least not as profitable as I suggest),

difference between fragmenting and bundling, even if running in favor of fragmented risk, is not large, rational insurers can pursue either model.

It has perhaps become something of a cliché that insurance is “affected with a public interest.”²⁹⁸ But that statement, though a bit trite, remains meaningful. Insurance is a fulcrum through which many human activities (commercial and personal) gain leverage to commence and succeed.²⁹⁹ It is no accident that the most industrialized and advanced countries of the world are also largely the most insured countries in the world.³⁰⁰ If regulators

there seems to be no doubt that they are quite profitable and quite capable of prudently taking on whatever increase risk may result from more comprehensive, socially useful underwriting and sales. *See* Kate Smith, *Feeling flush: despite Sandy, the U.S. reinsurance market remains rich in capital and capacity*, BEST’S REVIEW (Apr. 1, 2013), <http://www.thefreelibrary.com/Feeling+flush%3A+despite+Sandy,+the+U.S.+reinsurance+market+remains...-a0331805342>; *see also* *Travelers’ Q2 Profit Climbs 85% to \$925M; Auto Unit Layoffs Planned*, INS. J. (July 23, 2013), <http://www.insurancejournal.com/news/national/2013/07/23/299359.htm>; *Travelers Q1 Profit Up 11% to \$896M; CEO Says ‘We Will Keep Going’ on Rate Hikes*, INS. J. (Apr. 24, 2013), <http://www.insurancejournal.com/news/national/2013/04/24/289517.htm>; *Liberty Mutual’s 2012 Profit Jumps 132% to \$829M Despite Q4 Net Loss*, INS. J. (Mar. 1, 2013), <http://www.insurancejournal.com/news/national/2013/03/01/283292.htm>; Susanne Sclafane, *Insurance Ops ‘Shoot the Lights Out’ At Berkshire, Buffett Says*, CARRIER MANAGEMENT (Mar. 2, 2013), <http://www.carriermanagement.com/news/2013/03/02/101235.htm>.

²⁹⁸ *See* 20th Century Ins. Co. v. Super. Ct., 109 Cal. Rptr. 2d 611, 625 (Cal. App. 2d Dist. 2001) (“The field of insurance so greatly affects the public interest that the industry is viewed as a ‘quasi-public’ business, in which the special relationship between the insurers and insureds requires special considerations.”); *see also* German Alliance Ins. Co. v. Lewis, 233 U.S. 389, 415 (1914) (“[T]he business of insurance, it having become ‘clothed with a public interest,’ and therefore subject ‘to be controlled by the public for the common good.’”); *Daniel v. Tyrrell & Garth Inv. Co.*, 93 S.W.2d 372, 374–75 (Tex. 1936) (“The business of insurance generally is now recognized to be one affected by public interest.”); WASH. REV. CODE ANN. § 48.01.030 (West 1995) (“The business of insurance is one affected by the public interest”).

²⁹⁹ *See* Stempel, *The Insurance Policy as Social Instrument*, *supra* note 232.

³⁰⁰ *See* THE ORGANISATION FOR ECONOMIC CO-OPERATION AND DEVELOPMENT, GLOBAL INSURANCE MARKET TRENDS 2012 (2012), *available at* <http://www.oecd.org/daf/fin/insurance/GlobalInsuranceMarketTrends2012.pdf>.

put in place a level playing field for insurer competition, the insurance industry will do fine economically, just as it did in the wake of the work of Sawyer and others who championed bundled coverage as something good for insurers, policyholders, and society.

Excessive fragmenting of risk effectively reduces insurance protection and the certainty and confidence sought by socioeconomic actors. More bundled and comprehensive insurance products are more socially useful insurance products. Insurers should be more inclined to offer them, as they were during the mid-twentieth century, than they have been for the past quarter-century. Rather than engaging in a war with regulators (or legislatures or the courts), insurers would save disputing costs and serve the public interest (and, I continue to think, their bottom line) by moving toward a more comprehensive approach rather than fighting a rear guard action in favor of fragmenting risk.

The primary argument against the comprehensive approach appears to be that it does not do enough to fight moral hazard:

Research has identified five main tools that almost all insurers use to one degree or another: risk-based pricing; underwriting; insurance contract design; claims management; and, less frequently, loss prevention services. In addition, some insurer and their trade associations also engage in research and education and, sometimes even promote public safety regulation.³⁰¹

At first blush, these approaches seem to have more in common with fragmenting risk rather than bundling it. However, on closer examination, they can be used as well to support a comprehensive approach. For example, risk-based pricing can involve either fragmenting risk to calculate

³⁰¹ See Baker & Swedloff, *supra* note 118, accord CAROL A. HEIMER, REACTIVE RISK AND RATIONAL ACTION: MANAGING MORAL HAZARD IN INSURANCE CONTRACTS (1985); Ben-Shahar & Logue, *supra* note 241. But see Fitzpatrick, *supra* note 82 (finding that although it is not a rational “tool” as such, most insurers are highly motivated by anxiety about claims responsibility mushrooming out of control if insurers do not act to curtail risk exposures in response to adverse claim developments).

premiums more finely, or it can involve accurately assessing the claims the insurer will incur under a bundled approach and pricing the more comprehensive product accordingly.

Underwriting can be undertaken either with an eye to finely subdividing risks or with an eye to assessing the claims likely to be presented by comprehensive coverage. The risks may be larger under the latter approach, but so too should be the premiums received and corresponding investment return. When coverage is fragmented, this may avoid issuing coverage to a riskier applicant, but it also increases the risk that the applicant will forgo coverage and the insurer will lose premium dollars.

Insurance contract design such as the Swiss cheese limitations discussed throughout this paper can limit risk. And that can save costs. But so, too, can comprehensive contract design that eliminates much of the expense of assessing coverage under more fragmented products. More comprehensive products not only can command a higher premium, but also can be used for marketing advantage and easier actuarial calculation.

For similar reasons, claim management is likely to be easier and less expensive for the comprehensive insurance company as compared to its fragmented counterpart. Loss prevention services appear to be a useful response under either model. In fact, if the insurer provides bundled, more expansive coverage, it has an incentive to undertake broader and more far-reaching loss prevention policies that eventually should be to the insurers' monetary advantage.

Further, insurers can profit and enhance social welfare by means other than controlling moral hazard. To be sure, insurers cannot be so vulnerable to moral hazard that they fail, but neither is moral hazard their only concern. And neither is it essential that insurers drive moral hazard to its lowest point in order to succeed. But another way, insurers can suffer a good deal of moral hazard and succeed, just as they can suffer a good deal of adverse selection and expansion in liability while succeeding. In order to thrive, insurers offering comprehensive coverage need simply underwrite a large enough and diverse enough risk pool while collecting adequate premiums and investing wisely—provided that they are not losing business unnecessarily to fragmenting competitors. In that sense, I

propose a forcing of the comprehensive approach as necessary through minimum mandated coverage or limitations on exclusions.

VII. CONCLUSION

To a degree, insurance has lost its way in the modern trend toward more fragmented risk and restrictive coverage. Although such strategies may be profitable for insurers, they run counter to sounder risk management approaches as well as the history of insurance as reflected in the work of Elmer Sawyer and other architects of the CGL policy. Rediscovering the sound logic, public spirit, and business sense of this era can broaden and improve insurance overall, which would provide greater protection for policyholders and victims, efficiency in risk management and dispute resolution, and profit for insurers. Rather than being forgotten in the manner of a retired athlete, Sawyer deserves to be remembered and his approach again re-injected into the insurance game.