

How the Limits Apply in the CGL

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All insurance professionals need to understand how the limits of liability apply in the commercial general liability policy. Whether providing advice to a policyholder regarding the purchase of limits or in complying with the underlying requirements of an umbrella or excess liability policy, a working knowledge of how much will be paid is crucial.

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Section III of the October 2001 edition of the Insurance Services Office, Inc. (ISO), commercial general liability (CGL) insurance policy begins by making it clear that the limits shown in the declarations fix the most the insurer will pay regardless of the number of insureds, claims made, or suits brought or persons or organizations making claim or bringing suits. (No changes to this section are proposed in the December 2004 edition of the ISO CGL policy.) In other words, just because more than one insured person is named in a suit or a claim, more than one person or organization is making a claim or suit, or more than one claim or suit is filed does not mean the limits increase.

To illustrate, let's say a building contractor accidentally breaks an electrical cable, resulting in loss of utility service to several surrounding businesses. Each business suffering the loss of service brings a separate suit against the building contractor for loss of use and damage to inventory that has spoiled. In this illustration, the limit will remain fixed—the fact that there are multiple suits from multiple organizations does not increase the limit shown on the declarations.

Six Interrelated Limits

The CGL policy lists on the declarations six different limits. While the limits are separately listed, it is important to recognize that the limits are all interrelated. That is, payment of damages on one limit *will also affect another limit*. More on how this actually works later in this article.

Aggregate Limits

Two of the most important limits of the CGL are the aggregate limits. An aggregate limit is the most the insurer will pay during the policy period. Once an insurer is legally obligated to pay the full amount of the aggregate limit (either by judgment or settlement), the insurer has no further obligation to the policyholder during the remainder of the policy period for any subsequent claims or suits that are otherwise covered by the policy and that would be payable under that aggregate limit.

Exhaustion of an aggregate limit also extinguishes an insurer's duty to defend an insured against any subsequent suits that fall within the depleted aggregate limit. A key role of an umbrella policy is to "drop down" and provide coverage for claims that are not payable under the CGL due to an exhausted aggregate limit.

A Caveat

Extending by endorsement a CGL policy beyond a 12-month policy period for an additional period of less than 12 additional months will *not* reinstate the aggregate limits if the policy is extended after issuance. For example, if a 12-month CGL policy was extended by endorsement 5 months into the policy period to a 21-month policy period (an additional 9 months), the period to which the aggregate limits apply is extended to the entire 21 months.

In this situation, it is preferable to either write a 21-month policy period at policy inception or write the CGL policy to expire on its normal anniversary date and write a second short-term policy for the 9-month policy term. In either case, the aggregate limits would apply to the 12-month period and *separately* to the 9-month period. If a policyholder has an umbrella policy, the short-term policy option is generally recommended as umbrella insurers usually require unimpaired aggregate limits (no sums have been paid or are payable that reduce the aggregate limits prior to the umbrella policy inception date).

The General Aggregate Limit

This aggregate limit is the most the insurer will pay for all sums as damages because of bodily injury, property damage, personal and advertising injury *except* for those sums paid as damages because of bodily injury or property damage included within the products-completed operations hazard. The products-completed operations hazard is defined in the policy and a separate aggregate limit applies to such claims or suits.

Included within the general aggregate are damages paid under insuring agreements Coverage C—medical payments and Coverage B—personal and advertising injury.

Products-Completed Operations Aggregate Limit

This aggregate limit is the most the insurer will pay during the policy period for sums as damages because of bodily injury or property damage included within the products-completed operations hazard. As Coverage B—personal and advertising injury claims do not fall within the products-completed operations hazard, this aggregate limit only applies to bodily injury and property damage and then only for claims arising out of specified hazards.

The specified hazards are those described within the definition of products-completed operations hazard and are limited to bodily injury or property damage:

- That occurs away from the named insured's premises *and*
- Arises out of the named insured's products ("your product") that are no longer in the named insured's possession or the named insured's work ("your work") that has been completed.

While the definitions of "your product" and "your work" need to be consulted to fully appreciate what falls within the products-completed operations hazard, the above describes in general terms what types of claims fall within this aggregate limit.

The products-completed operations aggregate limit applies *independently* of the general aggregate limit. Sums paid under the general aggregate limit do not reduce the products-completed operations aggregate limit and vice versa. Consequently, under the CGL policy, an insurer's total liability or exposure in a policy period policy is the sum of the two aggregate limits.

A Metaphor

Some commentators have suggested that the aggregate limits be imagined as two separate large tanks of water. Piping from each tank flows into smaller tanks, each of which represents the four other CGL limits. Presume at policy inception the aggregate tanks are completely full, the other tanks (limits) completely empty.

Any time a claim is paid, the smaller tank from which the claim is paid must first draw the water from the larger aggregate tank, reducing the water level in the aggregate tank. Claims are paid on the policy until the aggregate tank is empty—in which case the aggregate is exhausted as nothing is left. Any further attempt to draw from that aggregate tank during the policy period will come up dry. That is until the policy renews and the aggregate tank is refilled (presuming renewal CGL insurance is available).

Personal and Advertising Injury Limit

For the offenses that fall within the definition of personal and advertising injury (and subject to the Coverage B exclusions), a limit is listed on the declarations as personal and advertising injury limit. If the insurer is legally obligated to pay sums as damages because of personal and advertising injury offenses, the most that the insurer is required to pay is set by this limit.

This limit is independent of the each occurrence limit. Hence, it is possible that an insurer may be required to pay *both* the personal and advertising injury limit and each occurrence limit.

The personal and advertising injury limit applies not by offense, but *separately* to each person or organization that sustains damages because of a covered offense or offenses. However, regardless of the number of persons or organizations claiming damages from a covered offense, or regardless of the number of offenses claimed during the policy period, the insurer is obligated to pay no more than the general aggregate limit.

Each Occurrence Limit

This limit is the most the insurer must pay for the sum of all damages under Coverage A—bodily injury and property damage and Coverage C—medical payments. Although a separate aggregate limit applies to products-completed operations claims and those claims for bodily injury and property damage that do not arise out of the products-completed operations hazard, the each occurrence limit does apply to all sums paid under Coverage A.

An Occurrence

Exactly what constitutes an occurrence has been the subject of massive amounts of litigation and even more extensive debate. Most of the dispute is related to fortuity and how it relates to insuring agreement of Coverage A—bodily injury or property damage. However, the "occurrence" definition (an accident, including continuous or repeated exposure to substantially the same general harmful conditions) also must be understood to grasp how the each occurrence limit is to apply.

An Example

A food processor improperly prepares a shipment of seafood, resulting in a contaminated food product that is ultimately sold to the general public. Over 25 people become seriously ill as a direct result of the food contamination and bring suit against the food processor. Is each illness (bodily injury) suffered a separate occurrence? Or is the faulty preparation of the seafood, the underlying cause of the illness, the occurrence?

Case Law

Legal authority is split on this issue. Further, slight variations in the facts of the case may result in different outcomes. The general trend, however, is for the courts to take one of two views. The first view is that *underlying cause* which directly resulted in the bodily injury or property damage is considered the occurrence and thus, in the above example, the faulty food preparation would be deemed to be one occurrence. The second view focuses on the resulting injury or damages, finding each injury or damage to be a separate occurrence. In the above example, the second view may find 25 separate occurrences, requiring the food processor's CGL insurer to pay up to the each occurrence limit for each person who became ill, subject to the general aggregate limit.

It should also be noted that the number of occurrences is likely to be determined in the same manner when applying a "per occurrence" deductible included on a CGL policy.

Damage to Premises Rented to You Limit

Coverage for Damage to Premises Rented to You is not provided by a specific coverage grant but rather by exceptions to certain exclusions found in Coverage A—bodily injury and property damage. The first exception provides coverage for property damage to premises, including the contents of the premises, rented to the named insured for 7 or fewer consecutive days *if* an insured is legally obligated to pay for such damage due to any cause *except* fire.

The second exception, formerly known as fire damage legal liability, provides coverage for damage only to the premises (not the contents of the premises) if an insured is legally obligated to pay for the property damage, but only if the damage is caused by fire. Any legal liability imposed on an insured must arise out of tort and not contract for either exception (and thus the coverage) to apply. In other words, if an insured is held liable solely due to an agreement to be responsible for the property or for damage to the property, there is no coverage.

The coverage granted by the exceptions noted above is subject to the Damage to Premises Rented to You limit listed on the declarations. The limit applies to any one premises and is a sublimit of the each occurrence limit. Therefore, any property damage paid under the Damage to Premises Rented to You limit will reduce the each occurrence limit for that same occurrence and will also reduce the general aggregate limit.

Medical Expense Limit

Coverage C is a separate insuring agreement that obligates the insurer to pay reasonable medical expenses (subject to the CGL terms and conditions) for bodily injury, caused by an accident, without regard to fault. Coverage C—medical payments is subject to the medical expense limit listed on the declarations. The medical expense limit applies separately to each person, but is a sublimit of the each occurrence limit and, as with the damage to premises rented to you limit, payments made under medical payments will reduce the each occurrence limit for that same occurrence and will also reduce the general aggregate limit.

The Water Tank Metaphor

To continue the water tank metaphor, again picture the two aggregate limits (general aggregate limit and products-completed operations aggregate limit) as tanks completely full of water at policy inception. Connected by piping to the general aggregate limit is a separate, empty water tank that is the each occurrence limit. We will call this connection valve #1. The each occurrence limit tank has a separate pipe connecting it to the products-completed operations aggregate limit tank which is connected by valve #2.

If a claim is paid within the products-completed operations hazard, the each occurrence tank is filled by using valve #2 and drawing down the products-completed operations aggregate limit tank. Any non-products-completed operations claims are paid by drawing down the general aggregate limit using valve #1. In either case, the most that will be paid in any one occurrence is the capacity of the each occurrence water tank. The personal and advertising injury limit tank is connected only to the general aggregate limit water tank—any claims paid as personal and advertising injury will be limited by the capacity of that tank for any one person or any one organization.

The personal and advertising injury tank is neither connected to the each occurrence limit tank nor connected to the products-completed operations aggregate limit tank. Payment of personal and advertising injury claims affect only the general aggregate limit.

As a sublimit of the each occurrence limit, the Damage to Premises Rented to You water tank is connected only to the each occurrence limit water tank. Likewise, the medical expense limit water tank is also connected, by separate piping, to the each occurrence limit water tank.

In order to pay a claim under either coverage, water must first be drawn down from the general aggregate limit tank using valve #1 into the each occurrence limit water tank and then drawn down into the Damage to Premises Rented to You limit tank for such claims or into the medical expenses limit water tank. Any claims paid under either coverage reduce the water left in the each occurrence limit water tank available to pay claims for that same occurrence.

Aggregate Limit Endorsements

The general aggregate limits can be amended to apply separately to designated locations or to designated projects. Depending on the number of locations or projects designated, these endorsements can greatly reduce the likelihood that a policyholder's general aggregate limit will be exhausted during the policy period.

Nick's Circus, Inc. CGL Policy – Limits of Liability

- \$ 2,000,000 General Aggregate Limit (Other Than Products-Completed Operations)
- \$ 2,000,000 Products-Completed Operations Aggregate Limit
- \$ 1,000,000 Personal & Advertising Injury Limit - Any One Person or Organization
- \$ 1,000,000 Each Occurrence Limit
- \$ 50,000 Coverage for Damage to Premises Rented to You Limit- Any One Premises
- \$ 5,000 Medical Expense- Any One Person

Assume the above limits and CGL policy dates of January 1st to January 1st.

1) Nick's Circus, Inc. puts on a production in Lincoln, Nebraska. Unfortunately, the tent Nick's Circus owns and set up for the production collapsed during a performance on January 15th, injuring 15 patrons.

- a) Ten patrons are willing to settle for having their medical expenses paid. What is the *most* Nick's insurer will pay for the ten patrons medical expenses?

\$50,000 (10 persons times \$5,000 each person)

- b) After settling with the ten patrons for the maximum Medical Expense payable under the policy, two other patrons file complaints, seeking damages of \$5 million each. What is the *most* Nick's insurer will pay to defend these two claims?

Defense expense is unlimited under CGL (until settlement or judgment).

- c) What is the *most* the insurer will pay in total for the injuries to these two patrons who have filed the complaint, assuming Nick's is found legally obligated to pay their demands?

\$950,000 - \$1,000,000 Each Occurrence Limit is reduced by the \$50,000 Medical Expense payment

2) Nick's Circus, Inc. moves on to Seattle, Washington and rents an entire aircraft hangar for two months for their next production. During a rehearsal on March 15th, the fire-eater accidentally causes a fire that does \$150,000 of damage to the hangar.

Assuming Nick is found legally obligated (in tort) to pay for the damage, what is the most that Nick's insurer will pay for the damage to the hangar?

\$50,000 – The Damage to Premises Rented to You Limit

3) The fire quickly spreads to a nearby restaurant, injuring two patrons and damaging the restaurant building.

Nick's Circus is found to be liable for \$100,000 of damage to the restaurant building and \$50,000 each for the injuries to the two restaurant patrons. What is the *most* that Nick's insurer will pay for damage to the building and the injuries to the patrons?

\$200,000 - \$100,000 for the restaurant building (the building is not in Nick's custody) and \$100,000 total (\$50,000 each) for the bodily injury to the patrons. This payment is still within Each Occurrence Limit.

- 4) Nick's Circus, Inc. decides to change their image and begins using a new name on July 20th, the Grand Apple Circus.

On July 23rd, The Big Apple Circus files a complaint against Nick for infringement of trade dress, a Personal & Advertising Injury claim.

A judgment is awarded against Nick for \$100,000 in damages. What is the most the insurer will pay for this claim?

\$100,000 – this is a Personal & Advertising Injury claim that is subject to a \$1,000,000 limit per person or organization.

- 5) In order to improve his flagging image, Nick decides to print and sell trading cards to the general public with pictures and information about each of his performers. On August 23rd, it was found that one of the cards was so sharp that it cut a buyer's hand, requiring fifteen stitches and causing the buyer, a world renown surgeon, to miss three months of work.

Nick is found legally obligated to pay for these damages as the card was found to be defective when it left his possession. The award was \$1,200,000. What is the *most* the insurer will pay for this claim?

\$1,000,000 – the Each Occurrence Limit applies.

- 6) Nick moves on to Worcester, Massachusetts and sets up his tent for another production. Similar to the January 15th incident, the tent collapses, injuring six patrons on September 25th.

Assuming Nick is legally obligated to pay for their injuries, what is the most that Nick's insurer will pay in total for the injuries to the six patrons?

\$650,000 is available for this claim.

The General Aggregate Limit has been reduced as follows:

Date	Amount	Type	Reduction of General Aggregate
1/15	\$50,000	Medical Expense	\$50,000
1/15	\$950,000	Bodily Injury Payment	\$950,000
3/15	\$50,000	Damage to Premises Rented to You	\$50,000
3/15	\$100,000	PD to Restaurant	\$100,000
3/15	\$100,000	BI - \$50,000 to each patron of restaurant	\$100,000
7/23	\$100,000	Personal & Advertising Injury	\$100,000
8/23	\$1,000,000	Products-completed operations Bodily Injury	No Reduction (Only Products-Completed Operations Aggregate is reduced)
TOTAL	\$2,350,000		\$1,350,000
9/25	\$650,000	BI to patrons	General Aggregate Exhausted After Payment of \$650,000

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