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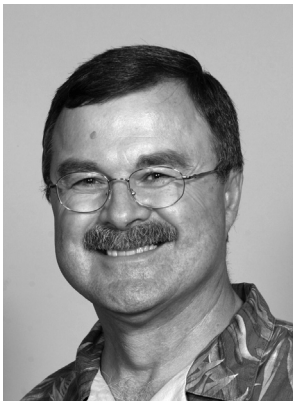
Chairman's Corner: What Kind of Coach Are You?

by Robert E. McHenry, CPCU, AIC, AIS

Coach: To train or tutor or to act as a trainer or tutor. A person who trains or directs . . . Dictionary.com



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My daughter is becoming a very good all-around basketball player. Mac is 11 years old, and 5'6" tall. Three years ago she played for a team that was blessed with a father and son-in-law coaching duo. These mentors focused on the basics of teamwork, ball handling, defense, and shooting. The two coaches noticed every improvement, good play, and used praise to teach and encourage Mac and the other players. They took her strengths and built the team around her position at pivot. They also worked on her weakness and improved Mac's shooting. She was named "most improved player." Ever since, my daughter has had the inner fire and love for the game.

Mac just finished the 2006 summer league season. Her coach knew and loved the game. Yet he failed to use his players' strengths and build on their weaknesses. Several of the girls had never played organized basketball before. No practice concentrated on the fundamental skills needed to function as a player or team member. There was no why, just the how. Instead of praising improvement, he yelled at them and questioned their abilities during practices and the games. The result was a winless record.

Which kind of coach are you? Do your players know the basics of coverage, damage, liability, subrogation, and salvage? Are they individuals or team members working toward a common goal? Are they aligned with the corporate mission and vision? Have you fueled their inner fire with praise for a job well done? What training did you give them on how the pieces of an insurance company fit together? Have you established the ground rules, set the playing field, gotten out of their way, and let them play the game? Are you a rousing good cheerleader? Would you want to play for a coach like you?

My first claims coach, Verne, taught me one basic of teamwork that sticks with me today more than 31 years later. "The car goes where you point it." I had questioned why a loss was assigned to me outside of my territory. That simple sentence meant I was part of his team and this was important. He had established the ground rules, set the playing field, and got out of my way. From that day on my car went where it was pointed.

Vince Lombardi began a new season by showing and then saying to his players "this is a football." John Wooden sat his team on the court and said "the first thing I'm going to show you is how to put on your socks." These men are two of the most successful coaches in our history. Why? Because they focused on the fundamentals, and their players did the basics better than anyone else.

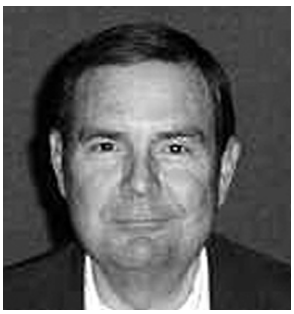
The CPCU Society is a team working toward the common goals of professionalism, ethical conduct, training, and high standards in the property and casualty insurance field. The CPCU courses help you learn how the pieces fit. The education that the nearly 26,000 Society members got from earning the designation makes a CPCU a valued player for any team. As a CPCU, we coach our peers and colleagues by our behavior and standards. ■

"They call it coaching but it is teaching. You do not just tell them . . . you show them the reasons."

—Vince Lombardi

Katrina—One Year Later

by James D. Klauke, CPCU, AIC, RPA



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I recently took some much-needed time off having worked seven days a week through the new year following Katrina. My wife and I decided to vacation at the beach in Gulf Shores, Alabama, which has now almost fully recovered from Hurricane Ivan in 2004.

We first took a driving tour of New Orleans. I was somewhat surprised to see so little damage repaired in the city north and east of the downtown area. These are the areas most affected by the flooding from the levee failures. While driving north and east along Interstate 10, we drove past mile after mile of apparently abandoned property. Major shopping centers with no sign of repair in sight. Small and large businesses closed, still heavily damaged, and exposed to the elements. An amusement park empty and silent on the last week of August before schools open. There were weeds already growing tall to hide most of the flood damage.

Then there are the homes, apartments, and condominiums. Most were fenced off to prevent theft and vandalism as the copper pipe and wire were still of real value. Exposed walls, doors, and windows abound from decay or being ripped off by the elements or would-be thieves or vandals. There is something very eerie about entire neighborhoods that have been totally abandoned.

We continued east on I-10 toward Gulfport, Mississippi. After leaving the interstate, I found most of the structures fully repaired and business open and operating. We stopped for a quick lunch at the McDonald's restaurant where I had lunch many times during the fall of 2005. Everything appeared back to normal prior to the storm.

I then drove to Highway 90 on the beach, and saw an entirely different scene. Few if any structures had been replaced, and almost none were in the process of repair. I looked for a Waffle House restaurant that I remembered to have a sign one week after Katrina that read, "We will be back." Sadly, it was not back, and the entire area was nothing but damaged foundation slabs and weeds.

As I drove along Highway 90, most of the homes that used to grace the coastline were still gone, and no indications of repair in site. The only work that was apparent was the removal of most of the debris and the replacement of some of the street signs. At best there was a scattering of dwellings and some commercial structures in the process of repair. I did see a large number of "For Sale" signs throughout the area. I would estimate that 40 percent of the coast is currently on the market.

The one class of structures that was repaired or in the process was the casino industry and the related hotels. Some were open for business, and the parking lots on a Sunday were near full. The ones still under construction had signs indicating they would be open before the end of the year.

Most of the roads and bridges were either repaired or in the process of repair. An exception was the Highway 90 bridges at Pass Christen and the Biloxi-Ocean Springs spans. Each was totally destroyed by the storm and waiting on funding from the state.

We continued our drive east to Gulf Shores, Alabama, our beachfront condo, and a week of relaxation on the beach. I had spent the better part of the fall of 2004 here handling Hurricane Ivan claims. The devastation was not as severe as Katrina, but it did come on shore as a Category 4 storm. The main difference was the speed as Ivan moved at a much higher rate of speed.

In this area I found only a few structures fenced off with no repair work evident. Most structures were fully repaired or totally removed. It was quite apparent that the only structures that can handle the beachfront property are the large condominiums and hotels built of steel and concrete. Wood structures just cannot handle the storm surges and winds that come on shore unabated. The wood structures do much better one to two blocks inland of the beach or behind large multi-unit structures.

Most, if not all, of the local businesses and commercial structures were fully repaired and back in full operation. All the debris was removed, the sand placed back on the beach, and grass visible on the lawns once again. What was also apparent was a large number of "For Sale" signs on the dwelling structures. I inquired with a real estate agent and was told most owners don't want to leave but don't like being unprotected. The cost of hurricane deductibles have doubled or tripled, and the premium has doubled or more. Insurance is also extremely hard to purchase as many carriers have pulled back to reduce the exposure.

My observations would suggest that it takes at least two years to fully recover from a large hurricane. Both Hurricanes Ivan and Katrina were Category 4 storms when they came ashore with Katrina dropping to a Category 3 almost immediately. Ivan claims are 99 percent resolved, and the restoration is about

98 percent. Katrina is at 80 percent claims settled; 70 percent of government assistance claims paid; and maybe 20 percent of damage repair completed.

See Table 1 for some startling numbers on claims paid to date. See Table 2 for ISO figures.

A lot of questions have been asked why New Orleans was so badly damaged, and why it is taking so long to restore the damage.

First there is the reason New Orleans was so badly damaged. It can be summed up in one word, **flood**. But, why did the levees fail so badly causing so much damage? The main reason is an infrastructure that was doomed to fail.

As we all know, New Orleans is located with most of the city below sea level. It is protected by a levee system and a system of water pumps that have kept the city safe and dry. However, they were built in 1745 of dirt and rock, and have been worked on many times since. The most recent work to improve the levee system was 1955 following their last failure from Hurricane Betsy, another Category 4 storm.

The soil under the levee system is a loose material much like peat moss and sand. Following the damage of Category 4 storm Betsy, the entire levee system was upgraded to withstand a Category 3 storm. That was the level of protection authorized by the Congress in Washington? This improvement was to install a six-inch concrete wall eight feet high on top of the existing earthen levee. This brought the total height to 15 feet above sea level. Category 4 Hurricane Katrina had a storm surge of 16 feet, as did Betsy in 1955.

Beyond the construction issue, there were three causes of the levee failures during Katrina. First, the water pressure saturated the soil beneath the levee. Remember that the soil is like peat moss consistency. The steel sheet piles driven in the ground to provide support for the six-inch, eight-foot high wall on top of this soil were driven down 20 feet or less. Once the water saturated the soil below the sheet pile, the pressure of the water surge just pushed the levee and the wall over or away. Some sections were found 30 feet from the original position still intact. The repair plan calls for the same construction with the sheet piles going down 80 to 90 feet.

Second, water just plain overflowed the top of the wall. This resulted in the soil supporting the wall on the dry side eroding away. Once enough of the soil eroded away, the wall had insufficient support and fell over from the pressure of the water surge.

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Table 1

New Orleans	Insured losses paid	$14,000,000,000
	National Flood losses paid	12,700,000,000
Mississippi	Insured losses paid	8,200,000,000
	National Flood losses paid	2,400,000,000
Alabama	Insured losses paid	1,000,000,000
	National Flood losses paid	300,000,000
Florida	Insured losses paid	700,000,000
	National Flood losses paid	100,000,000
	Total paid (June 2006 figures)	**$39,400,000,000**

Sources are State Insurance Departments, Federal Emergency Management Agency, and Risk Management Solutions as printed in *USA Today*.

Table 2
Catastrophic Hurricane Claims and Losses

	1999	2002	2003	2004	2005
Frequency	5	1	2	5	5
Claims	695,850	133,700	527,800	2,259,150	3,019,500
Personal Lines	73.90%	83.80%	82.30%	73.60%	69.20%
Commercial	17.20%	3%	4.10%	13.40%	9.40%
Vehicles	9%	13.20%	13.50%	12.90%	21.40%
Losses ($mil)	$2,315	$430	$1,775	$22,900	$50,055
Personel	39.40%	66.50%	74.90%	65.70%	49.50%
Commercial	55.60%	26.70%	14%	29.60%	44%
Vehicles	5%	6.70%	11.10%	4.60%	6.40%
Average Claim Severity ($mil)					
Personal	$1,773	$2,554	$3,061	$9,049	$11,860
Commercial	$10,769	$28,750	$11,376	$ 22,337	$ 77,592
Vehicles	$1,856	$1,638	$2,755	$3,626	$4,988

These figures are the ISO numbers through December 31, 2005, for all catastrophe claims.

Katrina—One Year Later

Continued from page 3

The third reason was just brute force of the water causing cracks in the concrete that eventually failed and broke. The obvious conclusion of engineers is "doomed to failure."

These same levees are being repaired in the same fashion as the original construction. The only changes noted are the sheet piles going down to firmer soil at least 80 to 90 feet deep. There is also some soil improvement. These changes will not prevent another failure when another Category 4 storm visits New Orleans. It is hoped that the next loss will not be as catastrophic. You see, these repairs only bring the levee system back to a Category-3-storm level of protection, as it was before Katrina.

Next comes the pump system to pump the water out of New Orleans, and keep it dry. This system was added to the levee system in 1912, and much of that original equipment is still in use today. They are still very efficient and able to pump water at the rate of 7,500 gallons per second. With the current number of pumps in place, they could drain the flooded city in 10 to 20 hours. So why did it take 20 days? Simple. The pumps were located below sea level, and the electrical system that operates them was even lower. No power, no pumping.

There was also the problem of the damage to the pumps from being under water. There are no spare parts for equipment manufactured in 1912. Parts for the repair had to be special ordered and fabricated. The repair is a mixture of old and new pumps, and the electrical systems have been relocated to the upper levels of the structures. The structures have some level of water protection now to reduce the flooding problem. The problem that will always remain is where to pump the water to get it out.

Though not involved in the cause or extent of damage, there is also the case of the Superdome. It was built in 1965 to withstand a Category 5 hurricane. It covers 130 acres of land and is 27 stories high. It did not fail until one of 12 roof dampers was blown off. This allowed wind to get under the roof material and peel it off. The styrofoam insulation and part of the decking followed. About one-third of the roof was gone following Katrina.

The second problem was a 100,000 people using it for weeks following the storm for shelter. It was designed for 70,000 people for four to six hours a week. The leaking roof shorted out some major electrical panels cutting off lights and pumps. The plumbing systems soon failed, and the bathrooms had to be closed. That's when the dome became a mess and all the problems began that were displayed by the media.

That was the situation in New Orleans, but Mississippi had its own problems. Its main problem was that it has many homes and businesses on or near the beach. Further, the eye of the storm crossed the coast at the Mississippi/Louisiana border so Mississippi received the full brunt of the storm surge and the highest winds, which are always on the east side. The flooding in Biloxi was 12 feet high, and the storm surge pushed structures from the beach inland about one half mile. The damage was along the entire coast of 80 miles, an area of high-density urban population.

Why have repairs taken so long and why have so many homes and businesses been abandoned? I believe the problem is governmental leadership at a local level that appears totally incompetent. Mayor Nagin and the New Orleans City Council are in total chaos. At the first anniversary of the storm, they still do not have a citywide plan for the reconstruction of the city. Many neighborhoods still do not have essential services, and there are no plans to return them soon. Why should residents rebuild when they cannot be assured of electricity or plumbing? It's a big part in why less than half of the 460,000 residents of New Orleans have returned.

Regarding the city plans, the following city plans have occurred since the storm:

1. January 11—The New Orleans Back Commission proposed a four-month time out to chart the future of New Orleans. The City Council objected and Mayor Nagin was cool. The result was a plan to shrink the city by not providing essential services to certain areas. This would require the residents to sell their property and move to more populated areas. On January 21, the Mayor rejected the preliminary plan.

2. On April 7, the City Council announced its plan with a $3 million budget. It never got off the ground.

3. On July 5, the mayor and the City Council joined forces with state officials to move a plan forward. They had a $3,500,000 grant from the Rockefeller Foundation to finance the plan. On August 3, consultants for the city were critical of the Rockefeller financed plan, and it fell through.

4. On August 22, with no citywide plan yet in place, the Louisiana Recovery Authority opened an office and started handing out grants for home repair from a pool of $7,500,000,000. Each grant is in the amount of $150,000. Forty thousand permits for rebuilding were issued that allowed residents to construct the homes exactly as they were prior to the storm. The Federal Emergency Management Agency suggested the new homes be raised three feet over the existing locations or foundations. This in spite of the fact that the Katrina flooding was as high as 16 feet.

Because New Orleans still has no master plan, reconstruction has been slow, and many residents have just decided not to return. Schools are an interesting indicator. Of the 52 schools that have opened, 32 are charter schools run by the parents of the children. They commented that for the first time, the children will be taught on new desks with new books and adequate supplies.

Table 3

Some interesting numbers from New Orleans supplied by the local media in June are the following:

Homes destroyed	102,879
Homes with major damage	201,491
Homes with little damage or already repaired	163,492

The Insurance Institute reports that less than 2 percent of insurance claims are subjected to suit or mediation. About 95 percent of the claims in New Orleans and Mississippi, or about 993,000 homeowners' claims, have been settled and paid. Unfortunately, it is the 2 percent mentioned above and those owners who did not have the foresight to buy insurance coverage that get all the headlines.

The insurance industry responded well to the largest hurricane disaster we have had in some time. Most open files are just awaiting the replacement cost claims that require repair costs to be incurred prior to payment. If there is a failure in this disaster response, it is the local, recently re-elected politicians. ■

Property Insurance Litigation in the Aftermath of Hurricane Katrina: The Early Results

by Daniel F. Sullivan, Esq., Gregory P. Varga, Esq., and Christopher F. Girard, Esq.

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In the December 2005 edition of *Claims Quarterly* (Vol. 23, No. 4), the authors provided an overview of several coverage lawsuits filed against insurers in the immediate aftermath of Hurricane Katrina that had the potential to dramatically impact the property insurance industry. Since that time, a number of those cases have worked their way through the court system and culminated in rulings, which are, by and large, favorable to the insurance industry. This article provides a brief report on some of the more significant decisions issued in 2006.

In the wake of Katrina, the principal target of the policyholders' bar was the so-called "flood exclusion" found in most homeowners and many commercial property policies. The plaintiffs in these cases argued that the exclusion was ambiguous and unconscionable, and that applying it to preclude coverage for property damage caused by storm surge and flood was against public policy. In 2006, the U.S. District Court for the Southern District of Mississippi addressed these challenges, and the early results favored the insurers. A prominent example is the case of *Leonard v Nationwide Mutual Insurance Company*, which was tried to District Judge L.T. Senter of the U.S. District Court for the Southern District of Mississippi.

The Leonards purchased a policy from Nationwide insuring their coastal Mississippi home, but did not buy flood insurance under the National Flood Insurance Program. The vast majority of the damage to their home was caused by storm surge, though some wind damage also occurred. The Leonards sued Nationwide after it offered to pay only a few thousand dollars for wind damage, and refused to pay for loss caused by flood. The policy contained a flood exclusion, which provided, in relevant part, as follows:

> We do not cover loss to any property resulting directly or indirectly from any of the following. Such a loss is excluded even if another peril or event contributed concurrently in any sequence to cause the loss. . . . Water or damage caused by water-borne materials . . . . Water and water-borne material damage means: flood, surface water, waves, tidal waves, overflow of a body of water, spray from these, whether or not driven by wind.

At trial, the Leonards argued that the flood exclusion of the Nationwide policy was ambiguous and unenforceable. The court rejected the Leonards' position, concluding that the flood exclusion was a "valid and enforceable term of the insurance contract" that had been "enforced with respect to damage caused by high water associated with hurricanes in many reported decisions." The court went on to rule, however, that the Leonards were entitled to be paid under the policy for that portion of the property damage attributable to the peril of windstorm, which the court calculated to be approximately $1,200.

The U.S. District Court's rulings in *Buente v Allstate Insurance Company et al.* and *Teupker v State Farm Fire & Casualty Company* addressed challenges to the flood exclusion similar to those presented in *Leonard*, but at earlier stages in the litigation. The plaintiffs in *Buente* and *Teupker* each alleged that their coastal Mississippi homes were damaged by Katrina's "wind, rain, and/or storm surge." In pretrial motions, the defendant insurers asserted that even if the facts alleged by the plaintiffs were true, the plaintiffs could not prevail as a matter of law because the damage was caused by water, not wind. In each case, the court concluded that the flood exclusions were valid and enforceable. In *Buente*, that conclusion was supported by the following rationale:

> The inundation that occurred during Hurricane Katrina was a flood, as that term is ordinarily understood, whether that term appears in a flood insurance policy or in a homeowner's policy. The exclusions found in the policy for damages attributable to flooding are valid and enforceable policy provisions . . . It is my opinion that the terms of the Allstate policy, specifically the "flood exclusions," set out above, are clear and unambiguous. Since the Court is not free to change or invalidate the unambiguous terms of an insurance contract (or any other contract), plaintiffs' motion for partial summary judgment will be denied.

As in the *Leonard* case, however, the court in *Tuepker* and *Buente* concluded that the plaintiffs were entitled to be indemnified for any property damage caused by the covered perils of windstorm and rain. "Again, these are fact-specific inquiries that must be resolved on the basis of the evidence adduced at trial."

In another important decision, the U.S. District Court for the District of Mississippi rejected an effort by the policyholders' bar to litigate flood exclusion cases through the device of a class action. In *Comer v Nationwide Mutual Insurance Co.*, the plaintiff attorneys sought to certify a class of 14 plaintiffs to represent all other "similarly situated" Mississippi property owners whose homes were damaged by Katrina and whose insurers had denied coverage based on the flood exclusion. The plaintiffs also sought to create several classes of defendants, including homeowners' insurers, and mortgage lenders that allegedly allowed homes to remain underinsured. The court refused to certify classes, concluding that class status was inappropriate given the necessity of a case-by-case examination of the facts. Of the putative class of plaintiffs, the court wrote: "Each property owner in Mississippi who had real and personal property damaged in Hurricane Katrina is uniquely situated. No two property owners will have experienced the same losses. The nature and extent of the property damage the owners sustain from the common cause, Hurricane Katrina, will vary greatly in its particulars. . . ." The court reached a similar conclusion with respect to the putative classes of insurers and mortgage lenders, noting that the particular insurance policies and mortgage agreements would have to be considered on their own merit. In the end, the court separated the 14 plaintiffs' lawsuits and required that each plaintiff reassert his or her claim in a new action against the particular insurance and/or mortgage company with which it had a contractual relationship.

Unlike their Mississippi counterparts, federal courts in Louisiana had yet to rule (as of October 1, 2006) on many pending challenges to the enforceability of the flood exclusion. That situation is expected to change soon, however. In several cases pending in federal court in New Orleans, the enforceability of the flood exclusion has been fully briefed on motion, and decisions should issue in the near future. Those cases include *Xavier University of Louisiana v Travelers Property Casualty Company*, and *In Re: Katrina Canal Breaches Consolidated Litigation*.

While the applicability of the flood exclusion has yet to be resolved under Louisiana law, the federal court in New Orleans has addressed another key issue raised in the wake of Hurricane Katrina: the applicability of Louisiana's Valued Policy Law (VPL) to claims involving flood and wind damage. The VPL provides, in relevant part that:

> Under any fire insurance policy insuring inanimate, immovable property in this state . . . in the case of total loss the insurer shall compute and indemnify or compensate any covered loss of, or damage to, such property which occurs during the term of the policy at such valuation without deduction or offset . . . .

The plaintiffs in *Chauvin v State Farm Fire & Casualty Company* had argued that because their homes were "total losses" and a portion of the damage was caused by the covered peril of windstorm, they were entitled to be paid the face amount of their insurance policies even though damage was also caused by the excluded peril of flood. After a careful review of the language of the VPL, the court concluded that the interpretation advanced by the plaintiffs would yield an absurd result:

> If the VPL has the meaning plaintiffs ascribe to it, an insured holding a valued homeowner's policy that covered wind damage but specifically excluded flood losses could recover the full value of his policy if he lost 20 shingles in a windstorm and was simultaneously flooded under 10 feet of water. The insurer would thus have to compensate the covered loss of a few shingles at the value of the entire house. . . . [and] would be required to pay for damage not covered by the policy and for which it did not charge a premium.

The district court also observed that the legislature could not have intended such a "commercially unreasonable" result when it enacted the VPL. Further, based on an examination of the legislative history of the VPL, the court concluded that it "was designed to regulate the valuation of a covered loss, not to create coverage for perils not covered by the policy." The plaintiffs are expected to appeal and the U.S. Court of Appeals for the Fifth Circuit should hear the case sometime in early 2007.

In conclusion, the insurance industry's early victories in cases such as *Leonard* and *Chauvin* provide hope that courts in the Gulf Coast region will remain faithful to, and will not ignore or attempt to modify, the clear terms of the policies in question. However, with literally hundreds of individual and class-action lawsuits slowly working their way through the courts of Louisiana and Mississippi, it is far too early to predict how the insurance industry will ultimately fare. Moreover, we have yet to see rulings from the state courts of Mississippi or Louisiana, where similar challenges have been advanced. The activity in these courts will be watched very closely. ■

Successor Corporate Liability for Defective Products

by James W. Roehrdanz and Nicholas W. Levi

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Corporate law principals dictate that when one company acquires the assets of a second company, the purchaser—or successor—does not assume the liabilities and debts of its predecessor. There are, of course, exceptions, but by and large in the commercial context, the exceptions to non-liability are narrow, and the creditors of a corporation are usually prohibited from collecting debts and judgments against successor purchasers. Particularities arise, however, when the claim against the corporation is not for a debt on a contract, but for liability for the manufacture or sale of a defective product. The traditional rule is that a company does not assume tort responsibility for defective products merely by acquiring the assets of the company that manufactured or sold the product. Transfer of liability has been limited to situations where the successor corporation is considered a mere continuation of the prior entity, evidenced by an alteration of the corporate form but retention of substantially the same stockholders, directors, and officers. Liability has also transferred through statutory or de facto mergers of corporations, in certain fraudulent transactions, and where there is a contract regarding transfer. However, many states have recognized that the narrow exceptions to the rule of non-successor liability leave claimants without legal recourse on otherwise valid product liability claims. There is an emerging trend toward expanding the scope of liability for product liability actions to certain arm's length transactions. In many jurisdictions, courts have held that where a particular product or product line transfers from one company to the next, the purchaser acquires legal responsibility for products manufactured and sold prior to the sale.

This article provides a broad summary of the rules for successor corporate liability when the claim is one for a defective product. Obviously, it is a collection of themes and general principles of law from multiple jurisdictions. Particular rules in certain states may vary greatly from the summary contained within this article.

Common-Law Exceptions Traditional to Claims of Successor Liability for Defective Products

Traditionally, courts look to whether the successor corporation is a continuation of the prior entity, such as through similar executive control and shareholders. These situations arise where the successor corporation is nothing more than the prior company under a new name, or where there is a statutory or de facto merger. Liability also transfers where there is an express agreement, or where the transfer constitutes fraud.

Assumption of Liability through Implied or Express Agreement

Where a purchasing company assumes obligations held by the selling company by agreement, those assumptions are enforceable. Conversely, where the contract says that liability is not to be transferred, it is not (assuming none of the other exceptions are satisfied).

Where claimants argue that a purchasing company has contractually assumed obligations for products it did not manufacture or sell, the case will turn on judicial interpretation of the asset purchase agreement. Often, liability for defective products sold prior to the asset purchase is deemed assumed without express language so stating. Language in a purchase agreement that calls for assumption of all liabilities and debts will usually be construed to include product liability exposure.[1] More specific contracts that itemize assumed liabilities or that reference classifications of the debts assumed by the purchaser generally do not extend to include liability for products manufactured and sold before the asset

purchase.[2] For example, agreements that limit exposure to "balance sheet" debts, or debts associated with traditional commercial transactions would not normally be construed to transfer liability for defective product claims. More difficult questions arise when courts are faced with the assumption of contractual warranties. Courts are split and in certain states, assumption of contractual warranties is extended to include product liability claims.[3]

Thus, if no liabilities are assumed by contract, or if the purchase agreement explicitly provides that the purchaser is not assuming liability for products sold prior to the agreement, liability does not transfer. However, where certain obligations are assumed by the successor, and the contract is silent with respect to product liability actions, courts will look to the similarities between tort actions and the liabilities expressly assumed to determine if the purchaser has implicitly agreed by contract to be liable for defective products manufactured or sold by the predecessor.

Fraudulent Transactions

Liability is also implicitly transferred where the purchase agreement is fraudulent or otherwise crafted to avoid debts and creditors. The hallmark of such transactions is a transfer of assets and/or product lines for inadequate consideration and for no apparent reason other than to avoid creditors.

De Facto Mergers

It is hornbook law that a statutory merger of companies transfers liability to the successor company. Courts have extended this rule to apply to de facto mergers, or transactions that are cast in the form of an acquisition or sale but have the economic effect of a statutory merger. The most important requirement for a de facto merger is a stock for asset purchase where the purchasing (successor) company uses its own stock as consideration for the purchase of some or all of the assets of the predecessor. Further, courts look to whether the selling corporation dissolves (or liquidates) shortly after the transaction as further evidence that the effect was a merger even if cast in terms of a purchase agreement. The effect of such a circumstance is that the owners of the separate prior companies are now owners of the purchasing company, which holds the assets of both prior entities. As the benefits of a merger are satisfied, courts will usually transfer tort liability for the products manufactured and sold by the predecessors.[4]

A stock for asset transfer is not mandatory, and courts have found de facto mergers in cash transactions; however, such circumstances are much less common.[5] In these circumstances, the courts retain the stock transfer as a factor, but state that evidence of additional factors, such as cessation of business by the seller shortly after the sale, and an assumption of normal business debts necessary to continue the business uninterrupted. While these courts have classified these as de facto merger cases, in reality, the analysis mirrors that of the emerging Continuity of Enterprise exception, which is discussed below.

What is important to note is that a stock for asset purchase, particularly if coupled with dissolution or liquidation of the selling company, presents very credible arguments for claimants to argue that responsibility for defective products has transferred to the successor corporation.

Mere Continuation of Predecessor

The Continuity of the Predecessor exception transfers liability in a corporate reorganization. In such a circumstance, one company technically transfers its assets to another, but in reality is merely altering its own form and structure. If the successor—even though a new corporation—is owned and managed by the same persons as the predecessor, liability usually transfers. One court has described such transactions as those that are "little more than a shuffling of corporate forms."[6]

The precise factors for the exception vary from state to state, but the primary concern is a continuation of ownership and control through retention of mostly the same stockholders and directors. Other factors include retention of the physical facilities, personnel, trademarks, and brands of the prior company. As ownership remains much as it was prior to the transaction, and additionally as the business is conducted in the same manner (often by the very same personnel), merely applying a new corporate "hat" will not usually terminate liability for products manufactured and sold prior to the change in corporate form.

Emerging Trends: Continuity of Enterprise

The above rule for imposing liability in corporate reorganization developed out of concern for allowing owners of a corporation to avoid their debts. This dovetails with the primary requirement: that the ownership remains substantially the same. In the absence of such a rule, the successor corporation obtains all of the success of the prior corporation (or of two different corporations in a merger), but would otherwise escape all losses accumulated before the sale. Without the Continuity rule, the same owners that accumulated the debts would be able to avoid them, yet otherwise continue their business uninterrupted.

Courts have recognized that this rationale is a bit limiting in the context of product liability claims. Notably, where a corporation sells its business (or merely a particular product line) and the purchaser continues the business of its predecessor without interruption, product liability claimants are potentially left with no recourse. The continuity of the predecessor and the de facto merger exceptions are not available as there is new ownership.

In response, many courts have crafted an additional exception, unique to the context of product liability claims: The Continuity of Enterprise. Continuity of Enterprise occurs when—although under new ownership—the successor

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Successor Corporate Liability for Defective Products

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corporation continues the business of the predecessor corporation with substantially the same personnel and equipment. The rationale often used to justify the rule is that as the purchasing company is acquiring the goodwill of the trademarks and products previously produced, it should additionally assume responsibility for their defects. Principal factors used in analyzing this exception include (1) continuity of personnel, particularly management; (2) continuity of the physical location and equipment; (3) continuity of trademarks and brand names; (4) and whether the purchasing company assumed those liabilities and obligations of the seller necessary for uninterrupted business operations.[7] In many ways, the Continuity of Enterprise exception can be classified as a continuation of a product line. Traditional rules have focused upon the continuity of ownership; but many jurisdictions have accepted arguments that continuation of the business of manufacturing a particular product or product line should transfer liability. Those that have not yet adopted the position are certain to face the arguments as cases develop.

Conclusion

There is often a reaction, among attorneys and insurers, that where a company did not build a product and did not sell a product, there can be no liability. This assumption does not bear out. Traditionally, only narrow situations permitted transfer of liability. However, inventive and competent claimants are going to argue that where a particular business is sold and the business continued in substantially the same manner, the present owner is liable for defective products dating back well before its purchase, or at least to the limits of jurisdictional limitation periods and statutes of repose. ■

Endnotes

1. *Kessinger v Grefco, Inc.*, 875 F.2d 153 (7th Cir. 1989); *Bippus v Norton Co.*, 437 F. Supp. 104 (E.D. Pa. 1977).
2. *Lockheed Martin Corp. v Gordon,* 16 S.W.3d 127 (Tex. App. 2000); *Shorb by Shorb v Airco, Inc.*, 644 F. Supp. 923 (E.D. Pa. 1986).
3. See *Valenta Enterprises, Inc. v Columbia Gas of New York, Inc.*, 455 N.Y.S.2d 996 (1982) (holding that agreement to assume all express and implied warranties excluded negligence claims but included strict liability claims as those have historically arisen out of the law of warranty).
4. *Sorenson v Allied Products Corp.,* 706 N.E.2d 1097 (Ind.Ct.App. 1999); In re Asbestos Litigation, 517 A.2d 697 (Del. Super. Ct. 1986).
5. *Klumpp v Bandit Industries, Inc.,* 113 F. Supp.2d 567 (W.D. N.Y. 2000).
6. *Savage Arms, Inc. v Western Auto Supply Co.*, 18 P.3d 49 (2001).
7. *Salvati v Blaw-Knox Food and Chemical Equipment, Inc.*, 497 N.Y.S.2d 242 (Sup. 1985), but see *Howard v Clifton Hydraulic Press Co.*, 830 F.Supp. 708 (E.D. N.Y. 1993) (holding that mere continuation in physical premises with change in name and much of management insufficient to impose liability).

Defensive Drivers

Bringing Golf Liability to the Fore

by Jesse A. Baird, CPCU, AIC

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Those in the business of handling insurance claims are aware that virtually all activities are fraught with liability hazards. A round of golf is no exception. Most golfers stand on the first tee, gaze out over the fairway, and look forward to a relaxing respite from the day's cares. An adjuster surveying the same scene, however, can't help but ponder: what legal calamities lurk within these deceptively idyllic vistas? What hidden litigious traps and impenetrable judicial thickets await the unwary? Should tragedy befall, who will pay damages? This article will answer these questions by exploring the liability threats specific to the game of golf that can result in claims against both golf courses and individual golfers.

Errant Golf Balls

It will come as a great relief to golfers and claims handlers alike to know that, when striking a ball, a golfer is usually not responsible for damage done by mis-hit balls. A golfer is only required to exercise ordinary care for people to whom danger can be reasonably anticipated. This means that golfers must be careful to avoid striking players in the intended line of flight of the ball; however, hooks, slices, or other errors do not necessarily mean that the player driving the ball is negligent. In fact, a golfer about to strike a ball is not even required to warn people not in the intended line of flight. The key to this defense is that—as in other sports where the risk of injury is obvious to players and spectators alike—the risk of getting struck by an errant golf ball is one that must be accepted by anyone playing the game. This principle has been stated and restated in a list of cases that reads like a truly bad day on the links:

- A man sliced out of the ninth fairway and into the parallel first fairway, striking another golfer and causing serious injury. The case was dismissed because there was no duty to warn persons not on the same hole or fairway, since the danger to those persons could not reasonably be anticipated.[1]
- A man waiting to play was struck on the head by a ball driven from a different fairway 220 yards away. The appellate court affirmed the dismissal of the suit, noting that "voluntary participants in sports activities assume the inherent and foreseeable dangers of the activity, and cannot recover for injury unless it can be established that the other participants either intentionally caused injury or engaged in conduct so reckless as to be totally outside the range of ordinary activity involved in the sport."[2]
- A golfer shanked a ball at a 90-degree angle, striking another golfer standing 30 feet away. The court dismissed the case, noting that the shot was "clearly unintended."[3]
- A man drove an errant shot that struck a member of his own foursome. The stricken player conceded the shot was an accident, but sued the defendant on the theory that he did not fulfill an alleged obligation to yell "fore." The court determined that since the plaintiff had been watching him make his swing, the defendant was not obligated to warn him.[4]
- The Hawaiian high court recently threw out a claim by a man who made a U-turn in a golf cart and suddenly emerged from behind a restroom directly into the path of the defendant's driven ball. That the defendant did not yell "fore" was not an issue, since the man who was struck was not within the line of play at the time the defendant made his swing.[5]

As in the cases above, most court decisions involving mis-hit balls that strike persons on a golf course emphasize the assumption of risk angle: the principle that anyone on a golf course, whether player, spectator, or employee, has assumed the risk of injury from flying golf balls, and that unless the driver of the errant shot was behaving recklessly, any injury is an unfortunate but inherent risk of the game. This is a crucial defense. It is also crucial to know that a related but separate defense, that of forseeability, is even more important in golfing situations. Indeed, reasonable forseeability is most often the key test of whether a golfer is responsible for the destruction wrought by his errant golf ball.

The focus on reasonable forseeability both broadens and narrows the defenses available to those whose golf balls cause damage and injury. It broadens them by protecting against claims by non-golfers who did not voluntarily assume the risk inherent in the game, but who nonetheless suffered the consequences of an incompetent shot. In a New York case, a golfer sliced his ball off the fairway and out of the course, where it struck a vehicle traveling on a roadway, shattering the windshield and injuring the driver. The court held that the golfer was not required to warn anyone not within the reasonable line of play, and that in order to be negligent he would have had to have aimed so badly that he unreasonably increased the risk of harm. The court noted that "even with the utmost concentration and tedious preparation that often accompanies a golfer's shot, there is no guarantee that the ball will be lofted onto the correct path." The court added that "There is no evidence that either defendant was careless or guilty of anything other than making an inept shot."[6] Further, the driver of the windshield-shattering ball was not required to yell "fore" because the driver of the stricken vehicle could not have heard him.

The principle of reasonable forseeability also applies to those who reside next to golf courses. In another New York case,

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Defensive Drivers

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the resident of a home next to a country club sustained a brain concussion when he was struck by a hooked golf ball while sunbathing on his patio. The court did cite the assumption of risk defense, and refused to determine that the plaintiff's rights as a homeowner had been violated, since "these invasions are the annoyances which must be accepted by one seeking to reside in the serenity and semi-isolation of such a pastoral setting"[7] (i.e., on a golf course). However, the court held that the accident was unforeseeable to the golfer (a 15-year old boy trespassing on a private country club) since the injured sunbather's home was separated from the fairway by 20 to 30 feet of dense rough and a stand of 60-foot-high trees. Taken by itself, the fact that the boy accidentally hooked his ball through that impressive quantity of foliage did not mean that he was negligent.

The focus on forseeability narrows golfers' defenses by making them responsible where the damage caused by a badly hit ball was accidental but should have been foreseen by anyone with common sense. In one case, a nine-year-old child was playing golf and allowed an adult golfer to play through. Even though the nine-year-old stood only slightly out of the path of the adult golfer's shot, the adult golfer took his swing and accidentally struck the child in the eye, blinding him. The court held that even though it was clearly an accident, the adult was negligent in taking his shot with the child so close to the intended path of his ball.[8]

Courts have allowed numerous cases to go to a jury to determine whether an injured party was within or close to the intended line of flight when a golfer struck the ball—in other words, whether the driver of the ball should have either warned those ahead or known better than to strike the ball when he did:

- The defendant drove his ball onto the fairway without a warning while the group ahead of him was still walking off the green.
- The defendant missed the twelfth green, hooking his ball onto the thirteenth tee and striking the plaintiff. The defendant admitted that the person struck by the ball was clearly visible and was only 20 to 25 feet away from the twelfth green at the time he took his shot.
- A caddy standing near a golfer's intended line of flight was struck in the head by a sliced ball.[9]

Again, the key to defending claims of this type is whether the defendant golfer should have reasonably foreseen that the shot could have resulted in harm to the injured party, at the moment the golfer took the shot. If harm to the injured party was clearly unforeseeable, there is no liability on the driver of the ball, regardless what mayhem the ball caused. If harm should have been foreseen by the golfer at the time the shot was made, the golfer is liable. In addition to being a legal principle, this is common sense for adjusters and golfers alike.

An adjuster handling a claim for injury from a mis-hit golf ball must focus on finding the positions of the plaintiff and defendant on the course at the moment the ball was struck. Once this is known, it must be determined whether the injury that occurred was foreseeable by the plaintiff. The less foreseeable the better, since in clear cases the courts frequently approve summary judgments in the defendant's favor.

Though the above discussion deals with golfers' liability, when tragedy befalls on a golf course, the course itself usually becomes a defendant as well. Courses are generally no more responsible for mis-hit balls than golfers. However, situations can exist where a safety hazard on the course can be alleged to have contributed to a golfing accident, particularly where errant balls are a frequent problem. If a course is aware of a problem with errant golf balls (say, a series of mishaps in which players are struck) caused by a specific condition and does not make an effort to fix it, the course could be held responsible for injuries under the law of premises liability.[10]

An adjuster faced with an errant ball claim against a golf course should first thoroughly investigate the site of the accident to discover if there is anything about the course that could have contributed to the occurrence of the injury. The adjuster will also need to find out if other, similar accidents have occurred in the past, and if the course had taken steps to correct the problem. If the course were aware of a problem with golf balls flying into an area occupied by patrons, the forseeability of the accident, and thus the negligence of the golf course, increases.

Golf Courses as Attractive Nuisances

There is another aspect of premises liability that is specific to golf: the fact that golf courses can be seen as gigantic attractive nuisances. An attractive nuisance, of course, is an inviting yet dangerous condition that may lure a passerby to potential injury. Golf courses contain many such "conditions"—ponds used but not intended for swimming, hills used but not intended for sledding in winter, and bucolic paths used but not intended for jogging.

If a swimmer, sledder, jogger, or other non-patron submits a claim for injury on the course, the adjuster must find out if the hazard that caused the injury was clearly marked as a hazard. The claim-handler must also determine whether the activity that resulted in injury was allowed or prohibited by the golf course. If the use of the course by non-patrons was prohibited, the adjuster must determine if reasonable efforts were made to prevent people from entering and using the course for unintended purposes. If non-golf activities are allowed on the course, the course must be maintained with these activities in mind. For a course to be exonerated in the event of a claim or lawsuit, all reasonable steps must have been taken to prevent an accident.

Golf Cart Accidents

Since golf carts cannot exceed 15 mph and generally drive on groomed fairways and cement paths, it would appear to the

casual observer that golf cart accidents are generally limited to alcohol-fueled bachelor party rounds and college fraternity golf tournaments. The casual observer would be wrong. According to the forensic engineering firm Technology Associates, there are approximately 9,000 golf cart-related accidents requiring emergency room treatment in the United States each year. The majority of these are due to braking, cart rollover, or passenger ejection.[11] One writer on the subject has noted that "the great bulk of litigation against golf courses and clubs for personal injuries arises from accidents involving golf carts."[12]

Sharp turns, steep hills, and driver error interact with golf carts' open design and lack of seatbelts to cause these accidents. A brief survey of recent mishaps leads the reader to believe that one would perhaps be safer on a motorcycle:

- A man suffered spinal injuries when he was pinned under a golf cart after flipping it over. He was proceeding down a steep, winding path when he locked the brakes on the cart and it skidded and toppled to the left. He claimed in his suit against the golf course that the path was too steep, and warnings of this were inadequate.[13]
- A man drove a golf cart up a service road to play his ball. Instead of returning down the service road, he left the path and drove straight downhill. He lost control of the cart on the slope, was thrown out, and died when he was crushed between the golf cart and a tree.[14]
- Two men were driving through a parking lot in a golf cart when the driver made a sharp left turn, tossing the passenger from the cart. The passenger sustained head injuries and sued the course and the golf cart manufacturer.[15]

Golf courses can be held responsible for such injuries if improper maintenance of a golf cart, poor path design or maintenance, or any other hazard or condition contributed to the accident. For example, a golf course has been held liable where a steep slope was considered unreasonably dangerous because there were no guardrails or warning signs.[16] Driver error can be a difficult defense to sustain if the path was dangerous or inadequately signed.

Even more troubling for those defending a golf course against such an injury claim, in some jurisdictions a cart has been held to be a "dangerous instrumentality," making the course renting the cart responsible for any damages done by its misuse.[17] The result of this, that driver error is no longer a defense in these jurisdictions, is bad enough. Even worse, golf courses can in certain cases effectively be made the liability insurer for each cart renter, making the course responsible for the behavior of its patrons while behind the wheel.

Handling golf cart accident claims is a matter of determining what proportion of driver error, improper golf cart design, inadequate golf cart maintenance, and improper golf course design and maintenance combined to cause the accident. In addition to getting statements from the driver and any witnesses, claims handlers must inspect the scene of the accident and determine if prior similar accidents have occurred. In addition, an engineering firm should inspect the cart, and golf cart maintenance records kept by the course should be inspected. An adjuster should always be on the lookout for situations where improper golf cart design caused or contributed to the accident, since if the cart manufacturer is partly or wholly responsible, the golf course's liability is reduced.

Golf courses are subject to all the liability shocks to which modern business is heir. Claims can flow from alcoholic beverages, come out of discrimination in operations or membership privileges, be engendered by sexual harassment, stem from environmental concerns (such as fertilizer use), and even spring from water rights issues. These risks are not specific to golf, and are outside the scope of this article. However—importantly for the claims handler—the courts do not look at claims of these types as skeptically as they do claims related to golf play.

Defendants in golf-play-related accidents, like those in other sports, benefit from the judiciary's approach that injury is always a potential byproduct of sporting activity, and that a person causing injury during the course of play is not negligent per se unless behaving recklessly. Thus while the test for negligence in individual golfing accidents is whether the injury was foreseeable by the defendant, it is almost always assumed that a plaintiff on or near the course assumed the risk of injury. This is an important protection for golfers who occasionally hook, slice, or shank their drives. And it makes the legal position of even the less than stellar golfer not a bad one to be in—something the claims-conscious should remember to help them relax while teeing off. ■

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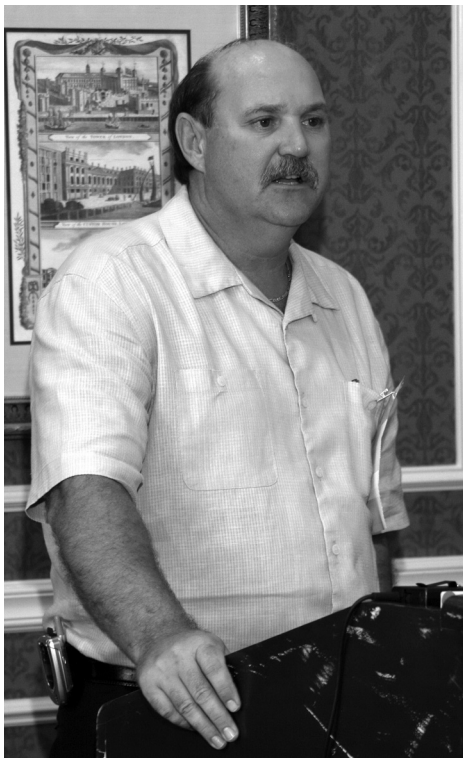
Claims Section Luncheon an Artistic Success!

The CPCU Society's Claims Section had a musical lunch meeting on September 10, 2006, at the Gaylord Opryland Hotel in Nashville, Tennessee. Leading and presenting at the meeting were **John A. Giknis, CPCU,** of ISO; **Tony D. Nix, CPCU**, of State Farm; and **Derek Crownover** and **Karl Braun** of the law firm of Hall, Booth, Smith & Slover in Nashville, Tennessee.

Crownover discussed coverage issues associated with intellectual property, specifically risks associated with the Nashville music industry. He explained the risks associated with writing songs and creating published music, subject to BMI review, and the perils associated with "borrowed" melodies and lyrics, with cases in point of Vanilla Ice and George Harrison, who were fined for using pre-published lyrics. He discussed the plethora of songwriters, and the odds of having a song performed by a major artist, and the process of songs being put on "hold" in anticipation of purchase. The discussion was very interactive (many in the audience of 52 seemed to be familiar with the music industry), and was very informative and entertaining.

■ *Claims Section members enjoy lunch at the 2006 Annual Meeting and Seminars in Nashville, TN.*



■ *Tony D. Nix, CPCU, was one of the leaders introducing the speakers.*

Karl Braun, a partner who is also a songwriter, added to Crownover's presentation by adding personal experience. Braun is an accomplished musician, and with percussion backup by our own Tony Nix, performed three of his songs.

As an added bonus, a booklet "Live Like You Were Dying"(written by Craig Wiseman with a forward by Tim McGraw) containing a CD of the same name was given to all attendees. The booklet and CD were made possible through contributions by numerous Claims Section Committee members and their employers. ■

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