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Nataša Petrović Tomić, PhD*

LIABILITY INSURANCE AS A (SOCIAL) RESPONSE TO THE CHANGING REGULATORY FRAMEWORK: FROM PROHIBITED TO COMPULSORY

The article analyzes the relationship between the institutions of liability and liability insurance, aimed at identifying the modalities of their interaction. Insurance indisputably affects the development and scope of tort law, but this influence is not one-sided. At the present development level it has been noted that liability insurance also plays an indispensable role in indemnity litigation. The development path of liability insurance shows that the developed legal order entails two mutually compatible systems. Whilst objective liability for damages is the response to numerous activities that render realistic the possibility of causing damage to others, regardless of whether the damage could have been avoided through cautious behavior, liability insurance is the response to the changed regulatory framework, which leads to liability reaching unprecedented proportions. Therefore, the author concludes that insurance does not threaten to substitute the principle of compensatory damages with the logic of loss-spreading.

Key words: *Liability insurance. – Indemnity. – Regulatory framework. – Professional liability.*

1. OVERVIEW OF THE HISTORICAL DEVELOPMENT OF LIABILITY INSURANCE

Liability insurance is one of the younger branches of insurance and recorded its greatest expansion during the 20th century. It is a subtype of property insurance and differs significantly from the insurance of

* Associate professor, University of Belgrade Faculty of Law, *nataly@ius.bg.ac.rs*.

belongings, even though both are in the same category of insurance. With liability insurance, the insurer protects the property of the insured from compensation claims by third parties (protection of the insured) and at the same time guarantees payment of compensatory damages to the injured party (protection of injured parties).[1] This reflects the *superiority* of liability insurance, as an insurance product with a dual-target function. The idea of this insurance consists of the insurer assuming the financial consequence of a certain event that caused injury to another party (Sanz Parilla 2010, 817–825; Lambert-Faivre 1981, 193–201). In other words, the insurance covers the risk of compensation for damages to third parties (Ćurković 2015, 8). This protects the property of the insured from potential liability, i.e. decrease, due to the obligation of indemnity to third parties (which, in addition to damages, commonly includes interest). Therefore, the Law of Obligations of the Republic of Serbia stipulates that in the case of liability insurance, the insurer is liable for damages caused by the insured event only if the third injured party demands compensation. Unlike other insurances, civil liability insurance *per definitionem* implies the involvement of three parties (Bonnard 2012, 10). Therefore it converts a bilateral relationship, which stems from the rules on liability for damages (*injurer–injured party*) into a trilateral relationship, including the insurer, who assumes the financial consequences of the harmful events.

The development of this type of insurance exploded in the late 19th century and experienced a renaissance in the early 20th century in economically developed countries. Why is this? The prevailing system of subjective responsibility rendered the purpose of liability and liability insurance incompatible. If liability is based only on culpability, the purpose of its existence is brought into question if the insured can be acquitted of it by concluding an insurance agreement. In fact, a liability insurance agreement was perceived as a means of securing immunity from liability; something similar to clauses on exemption from liability. In this sense, liability insurance was labeled as being immoral and socially unacceptable. Legal theory shared this view (Fontaine 2016, 515; Groutel *et al.*, 235; Jankovec 1977, 6).

Liability insurance may apply to the liability risk that threatens the private sphere (the best example is the insurance that the average insured encounters most commonly: motor liability insurance) or the risk of liability that affects businesses (corporate liability insurance). Namely, the consequences of the liability of business entities may jeopardize their further operation. By paying out compensation instead of the businesses who are responsible for the damages, the insurer allows for the unimpeded

[1] The originality of this type of insurance is reflected precisely in the fact that there must be debt of the insured to a third party, based on tort law. See: Abravanel-Jolly, 309; Groutel *et al.* 2008, 1081.

continuation of all economic activities and unimpeded economic growth. In this sense, insurance is discussed in the context of not only economic importance but also broader social significance. It has undoubtedly contributed to the acceleration of technological development, which is the most important factor in further progress. Nowadays environmental pollution liability insurance, product liability insurance, transport liability insurance in all industries of the transportation sector, etc., make insurance a top economic and social priority.

2. DEPENDENCE OF INSURANCE DEVELOPMENT ON THE SYSTEM OF LIABILITY

The significance of liability insurance was recognized only with the development of objective liability for damages.[2] Moving from a system of culpability to a system of liability, based on the produced risk, opened the door for the introduction of insurance that ensures transfer of the risk conceived in this manner. Actually, one could claim that these two systems developed in parallel with businesses, professions and activities that come with an increased risk (Karanikić Mirić 2013, 7). The changes that occurred during the second half of the 19th century in the system of liability for damages led to the development of liability insurance. With awareness of the need to accept another basis for damage liability, the idea started developing of a system that would serve to ensure compensation for all damages that are incurred even without anyone's culpability. Since its first appearance, liability insurance has remained inseparably linked to liability. It is our opinion that insurance should be perceive as the *public/social response to risk*. The moment that awareness developed of the justification for introducing other grounds for liability for damages, conditions were met to develop a system whose target function was linked to the amended rules of tort law (Merkin, Steele 2013, 3). The introduction of objective liability for damages provided conditions for the creation of purely objective liability risk, which is very insurable due to its qualities. Contemporary economics has developed over the decades, based on providing a diverse spectrum of services, which contributes to a sense of exposure to risk and fuels the development of liability insurance.[3]

Based on the general rules of tort law, the party that causes damages to another is required to provide indemnity. Since life in modern society

[2] The emergence of objective liability for damages did not imply the curtailment of subjective liability. In Serbian law—as is the case in other legal systems—both systems of liability exist, as does liability based on fairness. See: Konstantinović, 1154.

[3] Ćurković uses the term *vulnerability* to indicate increasing insecurity as an accompanying phenomenon of the modern way of life and conducting business. See: Ćurković 2015, 7.

includes participation in numerous activities that may lead to liability for damages or incurring damages, where most of these activities (working, driving a car, consuming food products, using dangerous devices, keeping animals, doing sports, using certain implements, etc.) is necessary, it is clear that the risk of liability falls on a large number of parties, both causing and suffering damages. Actually, all sources of increased hazard—as potential risks that are covered by liability insurance—can be generally classified into two groups: 1) owning (dangerous) items, and 2) performing (dangerous) activities.[4] Ultimately, when damages represent realization of the increased risk that was created by a party (by possessing certain items, keeping animals, or performing certain activities), a well-established legal order is recognized by the institutions that channel liability and direct it toward solvent debtors (such as insurers). Therefore it is no surprise that there is a proliferation of liability insurance, which is perceived as *a response to the growing risk of liability* in contemporary society (Konstantinović 1992, 1153–1163; Josserand 1992, 1164–1178; Stojanović 1992, 1179–1190). In so-called *claims society*, the question is no longer whether liability insurance is necessary, but rather which coverage is most auspicious. As pointed out by Ćurković, what was excluded from coverage until a few decades ago is now being insured at least as additional risk (Ćurković 2015, 14).

To summarize: *liability insurance varies within the limits of the civil liability of the insured*. Causing damages is the source of liability of both the insured and the insurer to the injured party. This is why theory recognizes that the civil liability of the insured is also the limit of the obligation of the insurer (Karanikić Mirić 2011, 687). If the liability of the insured is the assumption of the insurer's liability, they will not be liable if there is no party to whom the insured is liable. This does not imply that a relationship of equivalence exists between the liability of the insured and the obligation of the insurer. Departure from the rule that liability of the insurer implies the liability of the insured is introduced by law. The force of law in certain situations produces the liability of the insurer, even though an agreement has not been concluded (e.g. motor liability insurance kicks in even when the insured has not fulfilled their legal obligation to conclude an insurance agreement). Furthermore, an insurance agreement often includes limitations regarding the scope and breadth of the coverage, which is why insurance does not cover all the consequences of the civil liability of the insured (Šulejić 1992, 2261–2267). The effects of these limitations may lead to the insurer not covering all the damages for which the insured is liable or providing limited coverage. Therefore, it is not excluded that the obligation of the insurer may be lesser than the obligation of the insured to the injured party

[4] The greatest number of injuries that are the source of increased risk can be classified in one of these two groups.

(Konstantinović 1982, 496–505). These limitations are adjusted to the subject of the insurance, i.e. the type of liability covered. For this reason *liability insurance is considered an institution that to a certain extent releases from responsibility, which remains its conceptual basis*. This is primarily apparent in the case of compulsory insurance, where the insurer's obligation to the injured party is influenced to a lesser extent by the relationship that exists between the insurer and the insured.

Actually, liability for damages is a type of insurance.[5] This especially applied during the period prior to the emergence of liability insurance, as well as today, if conditions for the activation of the insurance are not met. If these conditions are met, liability is the gateway that leads to insurance (Merkin, Steele 2013, 251). Compensation and insurance embody different ideologies and the choice between them is not only a practical issue (conditioned by the level of development of the legal order), but also an issue of ideological approach. We undoubtedly advocate a combination of these systems. Only their complementary effect can adequately protect the interests of the injured party and ensure implementation of the principle of integral compensation.

3. AMENDMENTS TO THE REGULATORY FRAMEWORK: INTRODUCTION OF PROFESSIONAL LIABILITY AS AN INCENTIVE FOR THE DEVELOPMENT OF INSURANCE

It is our opinion that the current regulatory framework influences the development modalities of liability insurance to a great extent. In fact, the characteristics of the existing system of liability define the regulatory potential of liability insurance. As we have pointed out, this insurance appears as a response to the increasing liability risk in different occupations and activities. By constituting the level of responsibility for different professions, *the regulatory framework plays a decisive rule in defining/ quantifying the damages that should be covered by insurance* (Merkin, Steele 2013, 37). The best example of the influence of the regulatory liability framework on the physiognomy of insurance is professional liability insurance. Today there are numerous types of such insurance, whose common denominator is increasing confidence in professional advice– and service-providing individuals (and companies) as well as protection of the consumers of their services.

The fact that liability insurance today includes not only tortious, but also contractual liability, best speaks of how much it has changed

[5] Furthermore, it can be claimed that the institution of liability for damages is the predecessor of insurance. Its target function matches that of insurance, therefore the historical acceptance of this system opened the door to the development and subsequent expansion of (liability) insurance.

under the influence of the concept of professional liability. This change occurred as a response to the enormous liability risk that comes with certain professions. Historically viewed, liability insurance developed as an instrument for transferring risk from tortfeasor to the insurer, in the domain of non-contractual (indemnity) liability. It was believed that only this type of liability possesses the qualities necessary for insurance. Namely, it is based on general regulations on liability for damages (it is within the boundaries of the legal framework) and as such is aleatory. It was only over time, i.e. when standards of professional attention and the related concept of professional liability started developing, that the subject of liability insurance extended and started encompassing contractual (professional) liability.[6] This is why today it is incorrect to say that the subject of liability insurance is only non-contractual liability. Contractual professional liability is spreading at such a pace that certain professions have survived primarily due to insurance. Considering the fact that professional oversights (mistakes) are an integral part of different professions (i.e. contracts on performing certain jobs or providing certain services) and that they consist of the nonperformance of the assumed contractual obligation, the interest of the legal order to enable an extensive understanding of liability insurance is clear. It is for this reason that most legal systems include a significant number of compulsory professional liability insurances. It is the legislator's assessment that the protection of potentially injured parties—who use the services of various professionals—can be efficient only if professional risk insurance is compulsory.

4. MUTUAL INFLUENCES OF LIABILITY AND INSURANCE: INSURANCE AS THE COMPANION OF LIABILITY RISK

A historical approach to the study of liability insurance reveals not only that its development is directly linked to the development of objective liability for damages, but also that these two instruments are mutually linked and intertwined.

Even though indemnity is pushed into the foreground—as opposed to liability—insurance does not dismiss the idea of liability, even though it may happen that it changes or dislocates its meaning in the context of civil law. The links between liability and insurance run deep. "The responsible behavior of assured parties is of evident importance to insurers, and the subject of much industry attention." (Merkin, Steele 2013, 30). One of the fundamental rules in liability insurance is coverage for negligence. This emphasizes the significance of adhering to the standard of good faith, i.e. good business practices. This provides a meaningful and targeted connection between the rules on liability and

[6] For an overview see: Ćurković 2015, 40–44.

insurance. Furthermore, insurance enjoys its own legality in the sense of morality, which is closely linked to the correct basement on liability.

Over time, this branch of insurance started being perceived as an *instrument that provides a new dimension to civil liability for damages* (Eliashberg 2006, 17–32; Šulejić 1992, 2253–2267; Besson 1992, 2268; Sokal 1992, 2325–2338). It is no exaggeration to claim that civil liability insurance *increases* the reparative function of the rules on liability for damages.[7] However, its authority in contemporary indemnity does not end there (Fagnart 2013, 225–250). As pointed out by French theorist Andre Besson, there are three notable types of interference of insurance and liability (Besson 1992, 2257–2264).

First, the *development of liability through insurance*: this was especially the case with new forms of professional risk insurance, which were introduced at the same time as professional liability. In other words, *insurance meets the needs of new forms of liability*. The logic of the legal order was that it is easier to "tackle" new types of liability if insurance is introduced in parallel with them. Such an approach has proven to be justified in the case of compulsory insurance (such as motor liability insurance and various professional risk insurances). Regardless, objective liability for damages, as the general norm, was created in most legal systems in parallel with liability insurance. Also, the liability system improved thanks to the existence of insurance and the indemnity options.

Secondly, *development of insurance through liability*: "Every change in the system of liability has its reflection in insurance." This has proven true in the case of professional liability insurance. Due to consumerism and under the influence of consumer society, the legislators in many states kept extending professional liability. In the cases of certain professions such a legislative policy has led to excessive liability risk, which could be managed most efficiently through the introduction of compulsory liability insurance. Therefore, the legal regime of liability represented a direct incentive for the development of insurance. In most legal systems there is a significant number of compulsory professional liability insurances. It is the legislator's assessment that the protection of potentially injured parties—who use the services of various professionals—can be efficient only if professional risk insurance is compulsory.

[7] Even through insurance and liability are two separate categories (Ger. *Trennungprinzip*), they affect each other and become inseparably linked. The emergence of liability insurance is linked to the so-called *socialization* of liability, as an instrument that allows for the true application of rules on liability for damages, with the aim of protecting not only the injured parties, but also the entire community. The concept of the socialization of liability means transferring the burden of liability to all persons that make up the community, in the sense of being involved in the same business, using vehicles, etc. See Konstantinović 1952, 303; Šulejić 1967, 14–15; Besson 1992, 2269; Bonnard 2012, 11; Fagnart 1988, 419–448; Tunc 1982, 343–357; Delpoux 1992, 79–85; Frison-Roche 2000, 79–84; Mayaux 2011, 257–275.

Thirdly, the *corrective effect*, i.e. limitation of liability through insurance: liability is limited through liability insurance. Namely, insurers are not prepared to accept to cover a risk liability that is unlimited in scope or lasts excessively long, therefore they limit the duration of the risk in the terms of insurance. One of the common clauses in professional liability insurance is the claims-made clause (Petrović Tomić 2019, 520–522). This method of determining the insured case (only in liability insurance) developed out of the need to provide a time limit to the obligation of the insurer, who therefore conditions the acceptance of coverage of certain risks (e.g. consequences of environmental pollution, consequences of radiation, defective product damages, etc.) The claims-made clause was developed as a response to the extensively broad definition of professional (contractual) liability. Namely, insurers were not prepared to accept coverage of professional liability risks that last 10 or more years. By limiting the risk to the contractual period, the insurers could more easily assess the risk and calculate the premiums, which made insurance coverage more accessible.

Liability insurance devised in this manner can be observed not only as a corrective, but also as a counterbalance to the broadly defined liability. A good funded legal system features instruments whose combined effects provide a fine balance of mutually conflicting interests. Owing to such practices, in many occupations there have been legal interventions in the form of limitation of liability.

It is our belief that the list of interactions between liabilities and insurance does not end here, but that contemporary insurance law identifies several more modalities of interaction between insurance and liability.

Coverage for ordinary negligence based on liability insurance has influenced the interpretation of numerous duties that specify the standard of professional conduct in different activities. The significance of insurance is apparent from the fact that duties are always formulated as a legal standard, i.e. in an abstract manner and that their content is interpreted on a case-by-case basis (Merkin, Steele 2013, 214). It is evident that the mere existence of insurance is not sufficient to claim that there is a duty; duties are introduced by law and operationalized in practice. However, the role of insurance becomes prominent in the procedure of determining the content of such duties, because the courts rely on excluded damages and other limitations in order to determine the content of the specific standard of conduct.

The risk of common negligence is crucial in liability insurance: it establishes the limits of acceptable professional conduct in different professions. The insurance is in effect to the extent to which a party has abided by the professional standard, even in the event of an oversight and

despite all due caution. Since every party providing professional advice may experience an oversight due to negligence, the example of coverage of this risk shows the connection between the due attention of professionals providing advice or services and insurance. In our opinion, the treatment of this risk in insurance confirms the compatibility of tort and insurance law ("Negligence and insurance fit closely together", Merkin, Steele 2013, 62). In many cases parties that are professionally engaged in providing services or advice will not be held liable for common negligence (for example CEOs and members of corporate bodies). Insurance law follows the same logic in providing coverage for common negligence: if professionals are expected to act with due attention, then in the assessment of their liability it is crucial to separate common negligence from dereliction of duty. Insurance plays a significant role in this process.

As a consequence of the above mentioned, owing to the impact of insurance, the domain of illegal action is separated from acting in accordance with the rules of a given profession. This is closely linked to the notion of risk insurability. The acceptance and prevalence of liability insurance was affected by the fact that it covers all types of distorted behavior, with the exception of intent (Ćurković 2015, 9). Any form of conscious (intentional) violation of the law stems from the definition of risk as a crucial notion of insurance. Intent is excluded from coverage in all types of insurance.

Also, there is a noted combined effect of tort law and liability insurance in regard to the prevention of damages (Wandt 2010, 353). Insurance liability has evidently influenced the prevention of damages, since the terms of insurance stipulate in advance the prevention measures that the insured must abide by—under threat of sanction of compensation.

For understanding the preventive role of liability insurance, it is crucial that it is not comprehensive, i.e. that it does not cover the entire scope of liability of the insured, and therefore that it does not bring into question the preventive function of liability. Very prominent elements of the prevention of liability risk (insured's obligations, excluded damages, coverage limit, the *bonus malus* system, contraction of self-adherence, etc.) make liability insurance not only an instrument of protection, but also an efficient means of preventing high-risk business practices (Petrović Tomić 2011, 58). At the same time, liability insurance does not cover the entire field of the insured's civil liability, but also preserves the felony, administrative, disciplinary, status liabilities, etc.

This type of insurance is therefore an unavoidable factor of the financial security of natural and legal persons.[8] The need for liability insurance has started to increase with development of the culture of

[8] The philosophy of tort law has evolved significantly since the beginning of the 20th century. The primary target is no longer sanctioning of the tortfeasor, but rather

compensation in the 21st century (Ćurković 2008, 27). It is beneficial to all parties who may cause damage to someone, due to the activities they are involved in, to transfer the burden of compensation to the insurer. The reason for this is that the proceedings that the injured party may initiate against them, as well as the awarded compensation, may cause their ruin. It is clear that in this context liability insurance becomes a factor that determines the extent of the risk that the average citizen, service provider, or company may assume.

Even though there is, in a way, historical conditionality of the development of objective liability for damages and insurance, there is a line of thinking that states that the expansion of insurance gradually leads to the jeopardizing/reduction of the significance of the principle of tort. According to this reasoning, insurance threatens to substitute the principle of indemnity with the concept of spreading damages, which *in ultima ratio* "will reduce the law of tort to an empty shell." (Merkin, Steele 2013, 4). Our reasoning is quite different: we believe that insurance is part of a wider set of risk-related rules, which cannot be reduced solely to the principle of loss-spreading. What is common for all types of insurance is the reduction of insecurity. In this sense it is possible to distinguish a link between insurance and rules on liability for damages. Objective liability developed at the moment when the protection of the injured parties required that the issue of the culpability of the tortfeasor be put on the back burner and instead for the legal system to address the issue of who created the risk. Even though this purely technical principle is undoubtedly an important part of the insurance target function, we cannot view it separately from a private legal arrangement (agreement). Liability insurance is therefore inseparably linked and conditioned by the law of obligations (and tort law). It cannot be equated to the loss-spreading logic, nor is the function of loss-spreading free of the influence of tort law. Actually, insurance is the embodiment of the growing paradigm of risk management at all levels. Insurance law as such indicates to us the development trend of private law, aimed at it surviving and remaining an efficient means of protecting injured parties, as well as liable parties (who many not necessarily also be culpable, *ipso facto,* for the occurrence of the harmful event).

Liability insurance is the part of the legal order that contributes to the balanced functioning of the institution of private law.

compensating the injured party. See: Fagnart 1988, 135–157; Lambert-Faivre 2018, 438–441.

5. THE ROLE OF INSURANCE IN TORT LAWSUITS: THE DEEP-POCKET PHENOMENON

Insurance is able to affect the development of private law through a wide range of influences. Currently it is notorious that the influence of liability insurance is manifested most tangibly through the shaping of disputes pertaining to compensation.

Specifically, several regularities have been noted regarding the influence of liability insurance on the outcome of insurance disputes. Firstly, the presence of the insurer in the lawsuit is not a conceptually irrelevant factor (Merkin, Steele 2013, 7). They can appear in the lawsuit in different roles, which stems from the way that the dispute clause is formulated (Petrović Tomić 2020, 19–30). Thanks to it, a relatively swift conclusion of the settlement or acceptance of the indemnity claim by the insured is possible. The insurer may join the lawsuit as an intervener and ensure the intervention effect of the ruling. The insurer may therefore influence the outcome of the initiated lawsuit and render it more efficient than in the case when proceedings are held for the same matter, but without their participation.

Secondly, liability insurance plays an indispensable role in providing financial assistance to the insured, in the role of the defendant. Namely, in most cases the insured, based on this insurance, achieves not only coverage of the sum that is to be paid to the injured party, but also the costs of the defense. Consequently, the insured can count on a large fund and better-quality defense of their interests. Liability insurance traditionally is linked to an *indemnity function* that manifests itself differently than is the case with other property insurances. The protection that the insurer provides the insured consists of payment of the compensation for damages to the injured party, instead of the insured. Therefore, the assets of the insured are protected from compensation claims by parties who had been caused damages by the insured. Presently, however, the significance of liability insurance cannot be assessed without pointing out another function that it performs: the *legal protection of the insured*.

It is indisputable that the primary function of liability insurance is related to tort law and that it consists of protecting the insured's assets from compensation claims against them. However, in addition to economic protection, the insured also counts on legal protection. This is supported by the fact that the protection that insurance provides consists of the insured not having to bear the costs of the defense from the claims against them, as well as the indemnity that might be included in the ruling against them.[9] It is extremely important for the comprehensiveness of their

[9] When speaking of the function of liability insurance as the insurance of legal protection, we take into consideration legal costs and other justified costs of determining

protection that the policy includes a clause according to which the insurer is required to pay for the insured's defense costs in the course of the proceedings. This means that the insurer is required to cover the costs, regardless of the outcome of the proceedings.

In our opinion, the economic significance of liability insurance stems significantly from its character as a *passive insurance of legal protection* (Petrović Tomić 2011, 111). Even though it is indisputably predominantly liability insurance, this nature will not be evident in all cases. The indemnity nature of liability insurance is not manifested solely through the payment of compensation from insurance, but also through the financing of the costs of the insured's defense. Since the successful defense of the insured very often is concluded when judgment dismissing the claim is passed, it is appropriate to discuss the function of the insurance of legal protection. The Serbian Law of Obligations mentions "the expenses of litigation over the liability of the insured person", which the insurer covers within the limits of the insurance amount.

Thirdly, the "deep pockets" phenomenon, i.e. ruling on higher indemnity if it is known that the tortfeasor is backed by an insurer, is debatable. Namely, the issue of whether the defendant is insured is a private matter between them and their insurer.[10] The *inter pares* nature of liability insurance is taken into consideration in the case of voluntary insurance, while in the case of compulsory insurance the injured party has the option of choosing the defendant. Theory draws the conclusion that the existence of insurance often leads to lawsuits and conviction in order to ensure that the plaintiff receives indemnity precisely from the insurance. As far as the first instance is concerned, the filing of a lawsuit is influenced by numerous factors—including insurance. Insurance is viewed as something that parties may decide to invest in or they must obtain in certain situations, in order to facilitate the way that risk liability is managed. In this sense, knowledge that the tortfeasor is insured may induce the injured party to first attempt to reach an out-of-court settlement with them or their insurer. In well-established legal systems there are mechanisms that lead the injured party to follow a certain sequence of steps. It is only when this procedure proves inefficient that the injured party can initiate court proceedings. It is our opinion that insurance does not contribute to the taking of legal action any more than other factors do.

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the liability of the insured. Insurance also includes the costs of the third injured party pertaining to the litigation against the insured. Speaking of the latter cost category, they too are covered by the insurance, but we will not be discussing them within the scope of the legal protection of the insured.

[10] Presently there are no legal systems that include the obligation for the insured (defendant) to notify the injured party (plaintiff) of the existence of liability insurance. This information may be relevant only in the context of optional insurance. If such a risk is covered by compulsory insurance, this is known in advance. V.: Merkin, Steele, 384.

However, when it comes to the amount of compensation awarded, the role of insurance is certainly more prominent. Even though one might point out, as an argument against this view that damages claims have been tried in the past regardless of insurance, today the question whether the tortfeasor has insurance may be viewed as a circumstance that defines their financial situation.

For proper assessment of the "deep-pockets" phenomenon and its scope, one should start from the fact that the insurer will not, in any case, "pay the bill, whatever its amount." (Merkin, Steele 2013, 384). Insurers protect themselves from unlimited liability through two types of financial limitations. The first one is the insurance sum, which represents the coverage limit. The insurer will not want to make payment to the injured party beyond the insured sum. For any possible restitution that is not covered by the insurance, the injured party can only address the tortfeasor/ insured. The second type of limitation of the insurer's obligation consists of deductibles and franchises, which stipulate the insured's stake in the restitution (Petrović Tomić 2019, 457–459). Hence, the role of the insurer in compensation claims is complex and depends on the context.

Fourthly, when liability insurance policy clauses are interpreted, the court strives for this to be within the spirit of liability regulations. However, this influence of indemnity law is not straightforward. This is why when interpreting insurance policies, the courts are "conflicted" between two contradictory aspirations that are specific to the nature of this insurance. Namely, liability insurance is the only insurance product with a dual target function: it should not only reduce the insured's exposure to liability but also ensure funds for compensation of the injured party. The challenge is to interpret the policy in light of the hybrid nature of liability insurance, therefore it may happen that the courts take a different course, i.e. deviate from the rules on liability with the aim of acknowledging precisely the particularities of this insurance. Nonetheless, this is in the spirit of releasing liability insurance from tort law and the knowledge that when appraising insurance compensation, it is possible to deviate from the rules of this branch of law. An insurer who compensates the insured by deviating to a greater or lesser extent from tort law has at their disposal institutions that allow them to recuperate part of the funds.

However, even if the tortfeasor has liability insurance, this does not guarantee that it will be of use to the injured party, in the role of plaintiff. There are circumstances that compromise compensation by the insurer (Merkin, Steele 2013, 385). Firstly, the insurer may enter certain objections against the injured party as well as against the insured, which may lead to a reduction of the compensation from insurance.[11] Secondly, many

[11] In legal systems that don't recognize *action directa* as a general institution of liability insurance, the possibility of limiting compensation by entering an objection are

liability insurance policies contain a limit for the compensation (intended for the injured party) and a limit for defense costs. Finally, there must be a context of the claim and the subject insurance. The injured party cannot count on that coverage of the claim that extends beyond the limit of the tortfeasor's liability insurance.

However, a feedback effect is noted that insurance has on liability risk. Every insured risk evolves under the influence of insurance, and this is most apparent in judicial practice. Namely, in developed insurance markets it is noted that liability insurance has been leading to new trends in judicial practice in the past several decades. This by no means implies that someone will be found liable because they are insured. The influence of insurance on judicial practice is more subtle: conditions of liability will be assessed less rigorously if the defendant is insured (Bigot, Kullman, Mayaux 2017, 508). One should also not neglect the *effect of avoidance or mitigation of excessively strict legal solutions through insurance*. Liability no longer has the weight that it had prior to the development of liability insurance. Filing a subrogation request, even though in principle prohibited against members of the insured's family, becomes permitted as a result of insurance.

Over time insurance has led to the relocation of claims from the responsible party to the insurer, as the more solvent debtor (Fuchs, Pauker, Baumgärtner 2017, 363–370). In addition to allowing the risk bearer to sleep soundly, this trend has also led to certain negative consequences, e.g. certain forms of deformation of liability. Such influences have been noted especially in legal systems where determining the indemnity has been left up to the courts, as well as in cases when compensation is determined according to the principle of fairness (Ćurković 2015, 20). Even though the courts most often do not mention insurance even in the rationale of the decision, its influence is quite noticeable.[12] Furthermore, the knowledge that there is liability insurance is used by the courts to appraise the financial situation of the tortfeasor (the liable party), and the court might not reduce the sum owed by the liable party, even though their financial situation meets the requirements for the implementation of this instrument, solely because they are insured.

For this reason, we believe that liability insurance merits special treatment, compared to other insurances, and we propose the introduction of a special branch of insurance law: liability insurance law.

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much greater than in legal systems where the injured party cannot enter an objection that occurred after gaining the right to directly address the insurer.

[12] In countries such as Germany judicial practice is based on the principle of fairness, and the Federal Constitutional Court has confirmed that the existence of insurance is a relevant fact for deciding liability and determining the indemnity. See: Ćurković 2015, 22.

6. CONCLUSION

It is our conclusion that liability insurance, in its current form, was created and has endured as a response to the request for protection from increased risk. Historically viewed, liability is an older response to risk than risk transfer and over time there was a struggle over the issue of whether to allow the transfer of risk to insurers. For a long time, insurance was viewed with suspicion. The social climate and insufficient grounds and clarity of the institution of liability led to the favoring of liability over indemnity. In this sense, it is possible to divide the genesis of liability insurance into three phases. The first features the ban of such insurance, based on negating the moral qualities of transferring risk from the party that caused the injury to the insurer. This phase coincides with the period when the system of subjective liability for injury prevailed. The second phase is linked to the gradual acceptance of liability insurance, which was the consequence of understanding that the effectiveness of the legal order would increase if it accepted a system that accents compensation, while not negating responsibility. Finally, the third phase in the development of liability insurance was the introduction of certain forms of compulsory insurance, which occurred precisely in the domain of liability insurance. There is a notable overlap between the occurrence of new forms of insurance and significant commercial and technical progress. It is impossible to separate the allocation of risk that is generated based on regulations on liability and the increase in insurance, because many new types of insurance have emerged as a response to the changed legal landscape.

The development path that liability insurance has covered tells us that the founded legal order implies two mutually compatible institutions. While objective liability for damages is the response to numerous activities that render realistic the possibility of causing injury to others, regardless of whether the injury could have been prevented by caution, liability insurance is the response to the imposed regulatory framework, which enables liability to assume unprecedented proportions. The introduction of objective liability for damages meant creating liability risk, to which the regulatory framework responded by introducing compulsory insurance of that risk. Liability insurance supports the system of liability in achieving the set goals. In the 21st century this significant part of the legislation creates the conviction that the insurance market is a guarantee that efficient indemnity will be provided. Since the early 20th century, the risk of liability has become one of the most common risks, which creates a significant level of financial insecurity, whose compensation, in turn, is attempted through a system with the vocation of providing legal security. The culture of compensation—which can concisely be explained through the formulation that everyone seeks

opportunities to receive some form of compensation and which exposes service providers to potentially great liability—requires (compulsory) liability insurance.

It is undoubted that insurance is a factor that the parties take into consideration when deciding whether to file litigation for compensation, what their defense will be, whether and when they will conclude a settlement agreement, as well as how to exercise indemnity rights. Insurance is indisputably a procedural factor by its nature. Even though primarily a substantive legal institution, insurance today is a recognized procedural factor, whose scope under certain conditions may be limited by the circumstances of the specific case.

In conclusion, insurers that are involved in liability insurance, through their practices and indemnity litigation, are creating trends of the development/transformation of the institution of liability for damages. This leads to the creation of a type of indemnity insurance law, which is rather Americanized even in the European Union member states. It remains to be seen in which direction it will develop.

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