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Insurance Agent and Broker E&O 2013: The Year in Review, Part 2

by Peter J. Biging

Introduction

In last month's installment of this article, we discussed significant 2013 decisions concerning claims based on alleged "failure to advise," "failure to procure" and the interplay of the "duty to read" owed by insureds. This month's second installment will discuss significant 2013 decisions concerning: "causation" defense arguments; some creative claims and defenses, and how the courts dealt with them; the existence of a fiduciary duty; the economic loss rule; and some other miscellaneous issues. We'll also offer some thoughts on what this all means, and what agents and brokers (and lawyers who represent them) should do to respond going forward.

Causation

A critical defense available to insurance agent and broker E&O claims can often hinge on the argument that even though there may have been some negligence on the agent's/broker's part, there wouldn't have been coverage for the loss anyway. Among the significant decisions in 2013 with regard to this issue was the decision in *Hardy Oil Co., Inc. v. Nationwide Agribusiness Ins. Co.*,[1] In *Hardy Oil*, the plaintiff owned a petroleum bulk plant storage facility that contained five above-ground tanks that stored petroleum-based fuel for wholesale with on-site dispensing by transfer of the fuel from the tanks to a load-out rack via connecting fuel pipes that were located partially above ground and partially underground. Although it had property and liability coverage, it didn't have pollution liability insurance for the above-ground storage tanks. As a result, when there was a fuel leak from the underground pipes that required remediation, Hardy sought to recover the costs of same from the broker. Hardy's owner contended that while he had never asked specifically for pollution coverage, he had asked his broker if there was further protection he would recommend for the company. He contended that his failure to recommend the purchase of pollution coverage constituted negligence.

In the course of discovery, the broker noted that he did not recommend that Hardy purchase additional pollution liability coverage because: (1) such insurance can be expensive; (2) the inspections and testing necessary to qualify for such insurance can be expensive; (3) if the inspection or testing reveals a leak or environmental issue, then the state must be notified and an insured can incur substantial costs in rectifying the issue; and (4) in over 30 years as an insurance broker specializing in the petroleum insurance industry, he had never had a client request pollution insurance for above-ground storage tanks.

After discovery was taken, the broker moved for summary judgment dismissing the claim, on the grounds that even if you presume there was a duty to recommend that Hardy purchase pollution coverage for the above-ground storage tanks, Hardy could not prove that it was injured as a result. Specifically, the broker offered expert testimony that the Bulk Plant would not have qualified for pollution coverage for its above-ground petroleum storage tanks due to: (1) the facility's age; (2) the antiquated equipment/lack of documentation of any upgrade to the equipment at the Bulk Plant; (3) the absence of leak detection systems; (4) the absence of evidence of tank tightness testing/vessel integrity confirmation; (5) the absence of any evidence of environmental media sampling; and (6) the absence of any known site review/investigation reports.

In granting the broker summary judgment, the Court pointed out that even if it were to assume that the broker had breached a duty to advise Hardy of pollution coverage options, there was no evidence in the record that the Bulk Plant would have qualified for pollution liability coverage. While Hardy had offered generalized expert testimony that there were "more than 25 insurers [who] could have provided

pollution liability coverage which would have covered the loss," the Court found that a jury could not have concluded on the evidence before it that Hardy Oil could have obtained the coverage had it been recommended.[2]

Boiardi v. Freestate,[3] was a case that involved a similar question, but yielded a different result. In *Boiardi*, Plaintiff and her late husband were long-time clients of the insurance broker Mark Freestate. Through Freestate, they had purchased homeowners insurance for their home, and for seven years had paid all premiums due. However, after her husband passed away, Plaintiff missed the insurance premium payment, and the policy was cancelled. [Plaintiff contended that she made the payment by phone, but the Court in its decision stated that the insurer never received payment.] Thereafter, the bank that held the mortgage on her house ordered lender-placed insurance coverage be put in place, which cost substantially more and provided no personal property coverage. The bank sent notice of this, which the Plaintiff didn't receive until two months later when she returned from England.

Upon seeing the package advising of the lapse of her original homeowners coverage, Plaintiff called Freestate, who said "send me the documents and I will take care of this." While Freestate had a customer service representative working on trying to find replacement coverage, it was difficult because the prior coverage had been cancelled for non-payment of premiums, and the house was rated Protection Class 10, the worst rating a house can receive for access to fire protection services. The CSR had unsuccessfully contacted one insurer about replacing the coverage and was communicating with another when a fire broke out in the garage, causing extensive damage to the house and its contents, including two vehicles collectively worth over $400,000. After receiving a check for only the house's structural damage, the Plaintiff was so distraught she made a failed suicide attempt. She later sued Freestate and his agency for negligence, breach of fiduciary duty, negligent misrepresentation, and fraud.

At the close of discovery, the defendants moved for summary judgment on a variety of grounds, including that Plaintiff had failed to establish that replacement coverage would have been available; and so she could not prove that any misconduct on their parts proximately caused the loss. Further to this argument, they pointed to the underwriting hurdles posed by the cancellation for failure to pay premiums due, and the bad fire protection rating. They noted that one insurer that had been approached had declined the coverage. And they offered expert testimony that the other insurer that was considering offering coverage would have declined as well once the underwriter found out the prior policy had been cancelled for non-payment of premiums.

In rejecting dismissal of the claims on this ground, the court noted that:

> *Under Maryland law, a plaintiff does not need to show that an insurance policy was obtainable in order to prove that a broker's failure to procure such a policy caused her loss. Rather, availability of insurance is assumed unless the defendant proves its unavailability as an affirmative defense. In other words, "[t]he burden of proving nonavailability of insurance coverage is on the insurer or the broker, because it is an affirmative defense that is within the peculiar knowledge of those familiar with the market."* [4]

While Plaintiff had failed to offer evidence that another insurer would have actually provided replacement coverage, the fact that Chubb had originally insured it, another insurer was covering it under force-placed lender insurance, and a third was considering covering it—from which no affidavit had been obtained stating it would not have done so—provided sufficient grounds for finding that defendants had failed to meet their burden.[5]

Creative Claims

In *Noveletsky v. Metropolitan Life Insurance Company, Inc.*,[6] after her father died, the plaintiff was left with a $6 million estate tax liability, which she was paying off over time per agreement reached with the IRS. Concerned about planning for payment of these estate taxes upon her death, and the passing of the family business to her son, the plaintiff asked her best friend and ex-sister-in-law, a Met Life agent, to help her plan ahead. The friend/agent (Temkin) referred her to another MetLife agent (Silverman), who reviewed the plaintiff's financial information, reviewed what was still owed on the estate taxes, and recommended a MetLife whole life policy that had a $5 million death benefit and required annual policy payments of $66,750. It was projected that within 10-12 years between premium payments and dividends earned thereon, the policy would have enough cash value to cover the premium going forward. However, a decade later, the plaintiff learned that the projections were off and, in fact, the projection was now that payments would have to be made over an 18 year period. The plaintiff thereupon brought suit against Temkin, Silverman and MetLife, and, among others, asserted claims against Silverman for breach of fiduciary duty.

The case was referred to the Magistrate Judge for a report and recommendation concerning Silverman's motion for summary judgment, and the Magistrate Judge recommended dismissal. On review of the recommendation, and oral argument of Plaintiff's objection, the Court largely adopted the Magistrate's rulings, and specifically agreed that there was no basis for asserting a breach of fiduciary duty claim.

In reaching this determination, the court noted that in order to establish the existence of fiduciary relationship, it was necessary that evidence be presented of the actual placing of trust and confidence by one party in another, and a great disparity of position and influence between the parties in issue. Further, the court noted that under Maine law, to demonstrate the necessary disparity of position of influence, a party must demonstrate diminished emotional or physical capacity or "the letting down of all guards and bars." Here, although the plaintiff had alleged that Silverman's role went beyond that of an insurance agent to that of a

financial planner, the evidence presented was not sufficient. While there was no question that Silverman considered plaintiff's financial situation in making a recommendation regarding the insurance to purchase, the Court found that this was not evidence that he provided financial management services to her, and in considering her financial situation in this regard "he was no different from an ordinary life insurance agent attempting to fit a policy to the needs of his client."[7] While the Plaintiff argued that taking the Plaintiff's financial considerations into account, alone, should be sufficient to create a fiduciary relationship, the court stated, "[t]his Court declines the invitation to establish a fiduciary duty for insurance agents who take into consideration financial information of the insured."[8] And "[t]he fact that Silverman reviewed some of [plaintiff's] financial information does not convert the sale of an insurance policy into the provision of financial planning."[9]

Accordingly, while the plaintiff alleged a whole series of things Silverman allegedly failed to do (like "failing to undertake a financial needs analysis, failing to review the possibility of a universal policy versus a whole life policy, failing to advise her of the tax consequences of funding the recommended insurance policy through income from her companies," etc.), this was not sufficient, because evidence of a fiduciary relationship requiring Silverman to do any of these things had not been presented.[10]

In *5 Awnings Plus, Inc. v. Moses Insurance Group, Inc.*,[11] the trial court dismissed and the Appellate Division affirmed dismissal of a breach of contract claim based on a broker's recommendation that the insured take over the worker's compensation policy of a company it had purchased the assets of, and which the broker had handled its workers comp coverage for, after the purchased company ceased doing business. After the plaintiff allegedly signed an assignment of interest agreement based on the broker's recommendation, the plaintiff learned that the defunct company owed $12,000 in premiums. In affirming the dismissal on appeal, the Appellate Division noted that the Plaintiff's request that the broker procure the "best policy value" was not sufficient to create a duty to advise the Plaintiff concerning its insurance coverage. The assignment specifically provided that the Plaintiff would be responsible for the payment of any premiums or additional premiums which may become due up to the effective date of the assignment. Therefore, there was no breach of contract "because there was no specific request for coverage that defendant failed to meet."[12]

In *Cosper v. Farmers Ins. Co.*,[13] an insured couple tried to manufacture a claim based on an Oklahoma statute which provides that no insurance company shall knowingly issue any fire insurance policy which exceeds the fair value of the property, and requires insurers who knowingly put in place excessive coverage to reimburse the insureds for premiums paid in excess of the actual value to replace a property where it may be totally destroyed by fire and the actual replacement cost is less than the insured limits. Relying on this statute, the couple sued their insurer and agent for allegedly issuing a homeowners' policy with a replacement value that exceeded the property's actual cash value, causing them to pay higher premiums—even though they had not actually suffered a fire loss.

The insurer and agent successfully moved to dismiss plaintiffs' claims, on the grounds that they could not assert a claim under the statute because they had not suffered a fire loss, and that the claims did not state a common law claim for negligent failure to procure, misrepresentation, constructive fraud, or breach of fiduciary duty. Significantly, with regard to the negligent failure to procure claim, the court noted that plaintiffs had not alleged they had requested a specific coverage limit and defendants had disregarded the request and issued the policy in some other amount. In fact, there was no evidence the agent had played any part in setting the coverage limit. As to the misrepresentation claim, the court found that because the plaintiffs had not requested a specific amount of coverage, the defendants had no duty to provide "adequate insurance." Because they had no such duty, they also had no duty to advise plaintiffs that the coverage they accepted might exceed the amount needed to replace their home in the event of a total loss.

As to the "constructive fraud" claim, the court noted that constructive fraud is defined as a breach of a duty which allows one to gain advantage by misleading another. Since the defendant agent did not owe a duty in negligence or for misrepresentation, this claim also had no basis. Finally, as to the Plaintiffs' breach of fiduciary duty claim, the court noted that there was no evidence of a special relationship giving rise to a fiduciary duty of care regarding the amount of coverage to purchase.

Creative Defenses

On the defense "creativity" side of the ledger, in *Brandwein v. Butler*,[14] an owner of a yacht fell asleep at the wheel, had the vessel run aground, and ultimately was unable to salvage it. He had purchased it for $1.45 million, but put more than $1.5 million in additional monies into it in improvements. However, it was only insured up to the value of the purchase price, so that is all he recovered. He sued the broker for the difference, claiming the broker had represented itself as having special expertise in maritime insurance, and had only asked him the vessel's purchase price when he could and should have asked for and received insurance for the owner's improvements to the vessel.

Under California Insurance Law, codifying the maritime law doctrine of *uberrimae fidei* (utmost good faith), a purchaser of marine insurance is required to disclose all the information which he possesses material to the risk. Based on this, the trial court dismissed the claim. On appeal, the Court affirmed. Because the law required him to disclose this information, the court found that it didn't matter that the broker represented itself as being an expert in procuring maritime insurance, or that the broker didn't ask

if the vessel had for any reason increased in fair market value, or advise that it could be insured above the value of its purchase price.

Existence of Fiduciary Duty

As discussed in Part I of this article, in *South Bay Cardiovascular Associates, P.C. v. SCS Agency, Inc.*,[15] the court determined that there was an issue of fact regarding the existence of a fiduciary duty to advise the insured of changes to the company's employee dishonesty coverage, even though notice of the reduction in coverage had been sent to the medical group and received by the person responsible for insurance coverage there. On appeal, the Appellate Division affirmed, making reference yet again to the New York Court of Appeals decision in *American Bldg. Supply Corp. v. Petrocelli Group, Inc.*,[16] where the Court had stated: "While it is certainly better practice for an insured to read its policy, an insured should have the right to look to the expertise of its broker with respect to insurance matters."[17] Significant to the Appellate court's decision was the fact that not only had the medical group's employee who handled insurance coverage testified that she would not read policy language and notices (instead relying on the broker to tell her anything she needed to know), but she also testified that she had no special training in procuring insurance and did not choose coverage on her own, and the broker had told her he "did not expect her to read the insurance policies" purchased for the group.[18]

In another decision touching on the existence of fiduciary duties on the part of the agent/broker, *Micheau v. Hughes & Having an Insurance Agency*,[19] a Michigan appellate court discussed fiduciary obligations in the context of preparing the policy application. The court noted that because insurance companies rely on the truthfulness and completeness of the information on the application in assessing whether to issue a policy and on what terms, the accuracy of the information provided on the application is crucial. Accordingly, the court concluded that an agent owes a fiduciary duty of care in preparing the application, and violates that duty by negligently or intentionally misrepresenting relevant information in an insurance application, or by supplying patently incorrect information regarding how to interpret a question on an application in response to an insured's request for assistance.

Policy Reformation Based on Mutual Mistake

In *Caron v. Horace Mann Ins. Co.*,[20] after a homeowner purchased a homeowner's policy, her dog bit someone in the face, causing severe injuries. She thought, and the agent thought, the applicable limit was $500,000 because her dog was not a breed excluded under the policy. However, in fact, the policy limited all animal bite claims coverage to $25,000 per occurrence, and the agent never suggested otherwise to the homeowner. After a settlement between the injured victim and the insureds, the victim brought suit against the insurer arguing that the policy should be reformed based on mutual mistake. The trial court found in favor of the insured, but on appeal the Massachusetts Supreme Judicial Court reversed. In so holding, the court noted that the homeowner's mistaken belief regarding the coverage could not serve as the necessary predicate to a claim of mutual mistake. While the agent held the same mistaken belief as the insured, the absence of any communication of that belief to the homeowner robbed the mistake of the necessary mutuality.[21]

Duty to Notify Excess Carrier/Duty to Additional Insureds

In *Garner and Glover Co. v. Barrett*,[22] a contractor had procured a $1 million general liability policy along with a $1 million excess policy, and named the Atlanta Gas Light Company ("AGL") as an additional insured. After AGL was served with a Complaint, AGL sent notice to the broker that had procured the policy, and asked it to notify the primary carrier. The broker did, but did not notify the excess carrier. The excess carrier was subsequently put on notice after the claims adjuster on the primary policy advised that such notice should be given. The excess carrier at that point denied coverage based on late notice, but ultimately settled after litigation. AGL subsequently sued the broker for its legal fees incurred in having to sue for coverage on the excess policy, arguing that the broker should have also notified the excess carrier.

After the broker moved for summary judgment, the trial court denied the motion, but the appellate court reversed. In so doing, it found that in the absence of a voluntary undertaking by the broker performed negligently, it owed no duty to AGL, as an additional insured, to notify the excess carrier. Significantly, in so finding, the appellate court noted that it is not in an insured's interests to always and in all cases notify its excess carrier of potential claims.[23]

Assignment of Claims

In *DC-10 Entertainment LLC v. Manor Insurance Agency, Inc.*,[24] the court held that there is no prohibition in Colorado against an insured settling claims against it by an injured party by assigning its claims against its insurance broker for failure to obtain proper coverage for the injured party in exchange for an agreement to a specified judgment, and an agreement not to collect on that judgment against the alleged tort-feasor.[25]

Personal Liability for Professional Negligence

In *JT Queens Car Wash Inc. v. JDW & Associates, Inc.*,[26] the court denied a motion to dismiss an agent negligence claim against a corporate officer of the insurance agency in his individual

capacity because, while it is well settled that a corporate officer may not be held liable for the negligence of the corporation merely because of his or her official relationship to it, the corporate officer in this instance was alleged to have personally participated as an agent in issuing a certificate of insurance that negligently mis-identified an additional insured.[27]

Economic Loss Rule

In *Sharon Academy v. Wieczorek Ins., Inc.*,[28] the Court found that the "economic loss rule" does not bar claims against insurance agents and brokers for purely financial loss. In doing so, the court noted that the critical issue is whether a duty of care is owed independent of any duty imposed by contract. Because the Vermont Supreme Court has concluded that insurance agents/brokers owe a professional duty of care independent of any contract with their insureds, the court concluded in this case that the economic loss rule cannot be interpreted to bar the making of any claim based thereon. In so holding, the Superior Court noted:

> *By its nature, the injury for a failure to procure insurance will be solely economic: a lack of payment for financial losses. Thus, the economic loss rule, if applied here, would vitiate the existence of any such duty. Because Vermont recognizes such a duty, the court concludes that this creates a limited "professional duty" exception to the economic loss rule.*[29]

In reaching this determination, the Court noted that two other courts had recently recognized exceptions to the "economic loss rule" with respect to claims based on alleged negligence by a broker to procure insurance in 2013 as well.[30] This trio of cases seems to have dealt a substantial blow to the use of the "economic loss rule" as a defense to insurance agent/broker negligence claims going forward.

Statute of Limitations

In *Vinecourt Landscaping, Inc. v. Kleve*,[31] despite case law generally holding that a claim for professional negligence accrues when the act is committed, the court found that in insurance agent/broker negligence cases the claim accrues upon the sustaining of damages due to the alleged negligence. In so holding, and reversing a trial court ruling dismissing a claim against an agent as time barred based upon coverage purchased in 2006 leading to a substantially underinsured loss in 2011, the court noted "justice is not served where a tort dies before a reasonable person has an opportunity, in the exercise of ordinary diligence, to even *seek* redress."[32]

Conclusion

Moving forward, the key lessons to be learned from the trend in the insurance agent and broker E&O cases in 2013 are: (1) that the courts appear to continue to be increasingly open to consideration of arguments as to why "special circumstances" or a "special relationship" exist sufficient to give rise to a duty to advise; (2) while the "duty to read" is no longer an impenetrable defense to failure to procure claims, it remains a critical issue; (3) the economic loss rule appears to be in substantial retreat as a defense to negligence based E&O claims; (4) you generally cannot avoid potential personal liability for negligent conduct you participated in on the grounds that you were merely working as an employee of a corporation or as the agent for as disclosed principal; and (5) the courts are continuing the trend of applying a claim accrual rule for statute of limitations purposes that protects insureds from having negligence or breach of fiduciary duty claims against agents and brokers time-barred before the insureds even know they have sustained an injury and have an opportunity to seek redress. With several significant decisions already in 2014 in Florida and New York, it appears that this area of the law will continue to bear close watching going forward.

Endnotes

1. 2013 U.S. Dist. LEXIS 146163 (E.D. Ky. Oct. 8, 2013).
2. *Id.* at * 13-14.
3. 2013 U.S. Dist. LEXIS 138106 (D. Md. Sept. 25, 2013).
4. *Id.* at *29 (citations omitted).
5. *Id.* at 33-36. It is noteworthy, however, that the court found that an emotional distress claim was not available to the plaintiff. *Id.* at *59-61.
6. 2013 U.S. Dist. LEXIS 83762 (D. Me. June 14, 2013).
7. *Id.* at *21.
8. *Id.* at *23.
9. *Id.* at *24
10. *Id.* at 24-25.
11. 970 N.Y.S. 2d 158, 2013 N.Y. App. Div. LEXIS 5324, (App. Div., 4th Dep't 2013).
12. *Id.* at *161.
13. 2013 Okla. Civ. App. 78 (Okla. Ct. App. 2013).
14. 161 Cal. Rptr. 3d 728 (Cal. App. 4th Dist. 2013).
15. 963 N.Y.S.2d 688 (App. Div. 2d Dep't 2013).
16. 19 N.Y. 3d 730 (N.Y. 2012).
17. *Id.* at 736.
18. *South Bay*, 712-714, 963 N.Y.S.2d at 691.
19. 2013 Mich. App. LEXIS 849 (Ct. App. MI, May 21, 2013).
20. 933 N.E.2d 708 (Mass 2013).
21. *Id.* at 712-714.
22. 738 S.E.2d 721 (Ga. Ct. App. 2013), *Cert. den.*, 2013 Ga. LEXIS 770 (Ga. Sept. 23, 2013).
23. *Id.* at 723-724.
24. 308 P.3d 1223 (Colo. Ct. App. 2013).
25. *Id.* at 1227-1230.
26. 2013 N.Y. Misc. LEXIS 1353 (Sup. Ct. Suffolk Cty., Apr. 2, 2013).
27. *Id.* at 920.
28. 2013 Vt. Super. LEXIS 34 (Vt. Super Ct. Nov. 13, 2014).
29. *Id.* *10.
30. *See Cleveland Indians Baseball Co., L.P. v. New Hampshire Ins. Co.*, 727 F.3d 633, 640 (6th Cir. 2013); *reh'g. den.*, 2013 U.S. App. LEXIS 25591 (6th Cir. Dec. 23, 2013); *Tiara Condominium Ass'n Inc. v. Marsh & McLennan Companies, Inc.*, 110 So. 3d 399, 407 (Fla. 2013), *remanded by*, 714 F.3d 1253 (11th Cir. 2013).
31. 2013 Ohio App. LEXIS 6124 (Ohio Ct. App., Geauga County Dec. 31, 2013).
32. *Id.* at *14.

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