

YOU'RE NEVER 'FULLY COVERED' OBLIGATIONS AND LIABILITIES OF INSURANCE BROKERS IN PROCURING INSURANCE FOR THEIR CLIENTS

Nancy N. Potter Murchison & Cumming, LLP

A few years ago, I arranged to purchase a homeowners insurance policy from a major national insurance company. When I received the policy, I thought that the stated replacement value for the structure seemed low, particularly since I have an old house with unique architectural features. I consulted the agent, suggesting that the replacement cost limit needed to be higher. He sent me a letter stating in part, "You

have all the coverage you need to completely rebuild your house." My first thought was, "Now I do."

The insurance industry is in the business of providing peace of mind, and insurance brokers, whether independent or affiliated with an insurer, as the people with the direct relationship with the policyholder, often try to give that peace of mind. However, when a loss occurs, which for

some reason is not covered, the broker can be liable if the coverage available did not meet the insured's expectations. This article will discuss insurance brokers' duties, and some of the ways in which brokers can find themselves liable to insureds when the coverage turns out to be less than the insured expected.

Many times, of course, there is nothing a broker can do about the disappointed cov-

erage expectations: the loss is not insurable as a matter of law, or the claim set forth simply cannot be brought within the policy's insuring agreement. This does not prevent the broker from being sued for negligence or misrepresentation, especially if they have been overly sanguine in their assurances of full protection. Brokers who advise their clients that they are "fully covered" or can "rest easy" in an age of increasingly complex insurance policies are inviting the disappointment of their clients and lawsuits when it turns out that there is seldom, if ever, "full coverage" for any loss or claim.

GENERAL DUTY OF INSURANCE BROKERS

The basic duty of an insurance broker is simple to state: An insurance broker has the duty to procure the insurance coverage requested by the insured. *Jones v. Grewe* (1987) 189 Cal. App. 3d 950, 954; *Business to Business Markets v. Zurich Specialties* (2005) 135 Cal.App.4th 165. New York Courts have elaborated on that discussion of duty to note that the broker has the obligation to procure the coverage within a reasonable period of time, and, of course, advise if the coverage cannot be obtained. *Wied v. New York Cent. Mut. Fire Ins. Co.*, 208 A.D.2d 1132, 1133-1134 (N.Y. App. Div. 3d Dep't 1994)

Generally, the broker is not required to recommend additional coverage or higher limits. An insurance broker is neither a guarantor of coverage, nor a financial counselor or risk manager, and it is up to the insured to know its financial needs and condition. *Murphy V. Kuhn* 90 N.Y.2d 266 (1997) However, brokers have been found to have an obligation to be aware of the extent of their client's risk and make it clear to the insured whether or not that risk was covered. Moreover, once a discussion commences between the broker and the client as to what the client's needs and exposures might be, there is a potential risk that the broker will be considered a consultant and counselor, not merely a middleman, and will be found liable if the limits which are discussed turn out to be inadequate. *Paper Savers, Inc. v. Nacsa*, (1996) 51 Cal.App.4th 1090

A long-term relationship between the broker and the client, standing alone, is usually not enough to impose special duties on the broker. Even if the broker never advises an insured, over the years, that they might need to increase the policy limits of their policy to keep pace with inflation or their increased financial exposures, most courts have not held the broker to a heightened standard without more. *Murphy V. Kuhn* 90 N.Y.2d 266 (1997) *Trupiano v.*

Cincinnati Ins. Co., 654 N.E.2d 886, 889 (Ind. Ct. App. 1995) *Sandbulte v Farm Bur. Mut. Ins. Co.*, 343 N.W.2d 457, 464

EXCEPTIONS TO THE RULE

1. Misrepresentations:

The general rule of broker duty has been modified by many exceptions and limitations. First, of course, whatever insurance policy the broker procures for the insured must be adequately and correctly described to the client. A broker who advises the client of some, but not all of the exclusions contained in a policy of insurance can be liable when that one exclusion the broker didn't happen to mention becomes the cause of a loss. *Eddy v Sharp* (1988) 199 Cal.App.3d 858 A broker who promises to make sure the policy covers a particular kind of loss, and fails to read the policy when it is issued to make sure the loss is covered, only to find out later that the actual policy excludes that cause of loss, can also be liable.

Presumably, some of the insureds who find they lack proper coverage could have corrected the coverage before the loss had they only read their policies. While normal business prudence would suggest that a policyholder would at least attempt to read their policy, and ask questions if they didn't understand a provision or found an exclusion or limitation on policy limits, in many jurisdictions, the insured can recover even if, by reading the policy, he could have found the deficiency before there was a loss. Sometimes courts find that the necessary policy evaluation was beyond what was reasonable for a layperson, (*Portella v. Sonnenberg*, 74 N.J. Super. 354, 361 (App.Div. 1962), or that the normal rules of precaution are loosened in dealing with one's own insurance broker (*Riddle-Duckworth, Inc. v. Sullivan*, 253 S.C. 411, 423-424 (S.C. 1969); *Moore v. Kluthe & Lane Ins. Agency, Inc.*, 89 S.D. 419, 430-31, 234 N.W.2d 260, 266.) If the broker has affirmatively (if incorrectly) represented the coverage and exclusions of the policy, the insured can be excused for failing to read the policy himself. (*Eddy v Sharp supra* 199 Cal.App.3d 858) Some courts will allow a jury to decide whether the insured was contributorily negligent for failing to read the insurance policy, or at least verifying the broker's statements about the coverage provided. *Schustrin v. Globe Indem. Co.*, 44 N.J. Super. 462 (App.Div. 1957)

2. Special Expertise:

If the broker holds herself out as having special expertise and purports to advise the insured about the insured's coverage needs, the broker may be found subject to special duties. Thus, in a California case,

Williams v. Hilb, Rogal & Hobbs Ins. Service (2009) 177 Cal.App. 4th 624. the plaintiffs wished to open a Rhino Linings dealership and were told that a certain broker was "the go-to person" for taking care of those needs. That broker also assured the plaintiffs that she was an expert on the product necessary to satisfy dealers' needs. Plaintiffs placed themselves in her hands and she procured an insurance package which failed to cover plaintiffs' workers' compensation exposure. The court held that since the broker held herself out as an expert who would procure all the insurance they might need, they were entitled to rely on that. A South Carolina case noted that if the broker voluntarily assumes a duty to advise the insured, he may be liable for failure to use reasonable skill and care in explaining the policy or counseling the insured. (*Trotter V. State Farm Mut. Auto. Ins. Co.*, 297 S.C. 465, 479 (S.C. Ct. App. 1989)

In addition, if the broker is compensated for consultation and advice, the broker can be held to have thereby assumed additional duties. *Sandbulte V. Farm Bureau Mut. Ins. Co.* 343 N.W.2d 457 (1984).

While brokers may indeed choose to develop expertise in the insurance needs of a particular industry, they may thereby subject themselves to additional liability exposure if the insurance packages they advise their clients to purchase do not cover all of the exposures which tend to arise in those industries. *Third Eye Blind v. Near North Entertainment Ins. Services* (2005) 127 Cal.App.4th 1311.

CONCLUSION

A reasonable policyholder should not rely completely on a broker to assure that the coverage the broker obtains is adequate, nor should a broker make representations that the coverage procured will always meet the insured's needs. Over-promising and lack of diligence can leave an insured without needed coverage, and expose the broker to liability. As always, common sense and due care are in order.



Nancy N. Potter is an Associate Partner in Murchison & Cumming, LLP's Professional Liability and Insurance Law practice groups, handling the defense of brokers and agents for errors and omissions, doctors, medical practitioners and lawyers; complex insurance litigation; and insurance bad faith defense. Ms Potter also handles property coverage matters.