Agents E&O Standard of Care Project

Michigan Survey

To gain a deeper understanding of the differing agent duties and standard of care by state, the Big "I" Professional Liability Program and Swiss Re Corporate Solutions surveyed their panel counsel attorneys. Each attorney was asked to draft a brief synopsis outlining the agents' standard of care in their state. They were also asked to identify and include a short summary of the landmark cases. In addition, many of the summaries include sample case studies emphasizing how legal duties and issues with standard of care effected the outcome. Finally, recent trends in errors in the state may also be included.

This risk management information is a value-added service of the Big "I" Professional Liability Program and Swiss Re Corporate Solutions. For more risk management information and tools visit www.iiaba.net/EOHappens. On the specific topic of agents' standard of care check out this article from the Hassett Law firm, our E&O seminar module, and this risk management webinar.

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STATUS OF THE STATE OF THE LAW ON THE STANDARD OF CARE FOR INDEPENDENT INSURANCE AGENTS IN THE STATE OF MICHIGAN

Contrary to popular belief, the state of the law in the State of Michigan pertaining to an independent insurance agent's standard of care is in a state of uncertainty. Following the Michigan Supreme Court decision in *Harts v Farmers Insurance Exchange*, 461 Mich 1 (1999), it was generally believed that an independent insurance agent, not acting as a retained insurance counselor, did not owe a duty to advise a potential insured about the adequacy of insurance coverage. Subject to four limited exceptions, an agent's job was merely to present the product of his principal and to take such orders as could be secured from those who wanted to purchase the coverage offered. The Supreme Court in *Harts* also went so far as to modify the "special relationship" test that had been applied in situations where a longstanding relationship existed between an agent and an insured. The Michigan Supreme Court refused to subscribe to the proposition that a special relationship existed between an agent and an insured because of the length of the relationship and instead, modified the "special relationship test" so that the general rule of no duty changed only when one or more of the following factors were present: (1) the agent misrepresents the nature or extent of the coverage offered or provided, (2) an ambiguous request is made that requires a clarification, (3) an inquiry is made that may require advice and the agent, though he need not, gives advice that is inaccurate, or (4) the agent assumes an additional duty by either express agreement with or promise to the insured.

The decision in *Harts* was uniformally followed until 2008 when a panel of the Michigan Court of Appeals decided *Genesee Food Services, Inc. v Meadowbrook, Inc.*, 279 Mich App 649. In this case, the defendant Meadowbrook was an independent insurance agency. This contrasted with the agent in the *Harts* case who was a captive agent for Farmers Insurance Exchange. In noting that Meadowbrook was an independent insurance agency, the Court of Appeals ruled that the agent's primary *fiduciary duty* of loyalty rested with the plaintiffs who could depend on this duty of loyalty to ensure that the defendants were acting in their best interest, both in terms of finding an insurer that could provide them with the most comprehensive coverage and an ensuring that the insurance contract properly addressed their needs. Thus, the state of the law in Michigan went from a "no duty to advise" standard to a "fiduciary relationship" standard depending upon whether the agent was a captive agent or an independent insurance agent.

Four years later, in an unpublished Michigan Court of Appeals decision titled *Deremo v TWC & Associates, Inc.*, a separate panel of the Michigan Court of Appeals followed the *Genesee Foods* decision and distinguished the *Harts* decision as it applied to independent insurance agents. The Court in *Deremo* noted that from the *Harts* decision, it was clear from the facts that the defendant insurance agency was an exclusive agency because it only represented one insurer. The Court noted that the Supreme Court specifically used language describing an exclusive agent when stating the no-duty rule: "An insurance agent *whose principal is the insurance company* owes no duty to advise

a potential insured about any coverage." The Court therefore read the *Harts* no-duty rule as only applying to exclusive insurance agents. The Court then went on to look to the *Genesee Foods* decision in which the Michigan Court of Appeals specifically addressed the duty of an independent insurance agent as distinguished from that of an exclusive agent. Finding that TWC's agents were independent agents, the Court of Appeals ruled that *Genesee Foods* governed and that it was incumbent upon TWC's agents to provide its customer with the most comprehensive coverage and ensure that the insurance contract properly addressed the insured's needs.

To complicate the issue, several panels of the Michigan Court of Appeals have issued unpublished opinions dealing with independent insurance agents where they followed *Harts* and disagreed with the decisions in *Genesee Foods* and *Deremo*. In one recent decision decided in 2014, *Estate of Marine Richardson v David Grimes, Jr. and Quality Insurance Services, Inc.*, a panel of the Michigan Court of Appeals ruled:

> "Although *Harts* involved a captive agent rather than an independent agent, we conclude that the limited exceptions provided by our Supreme Court regarding the duty to advise concerning coverage apply equally to captive and independent agents for the reasons stated in *Nokielski v Colton*, unpublished opinion *per curium* of the Court of Appeals, issued January 4, 2011, which we find persuasive and adopt as our own."

These varying Court of Appeals decisions regarding the applicability or non-applicability of the *Harts* decision to independent insurance agents has allowed for uncertainty in determining the precise standard of care for an independent insurance agent. The "no-duty to advise" standard with the four limited exceptions allows an independent insurance agent to act as an "order-taker" in most situations where there is no interaction between the insured and the agent as to the adequacy of coverage. On the other hand, the *Genesee Foods* and *Deremo* decisions create a very high standard by raising the agent's standard of care to a fiduciary level which requires an independent agent to ensure that his or her customer is offered and provided "the most comprehensive coverage" that properly addresses the insured's needs. Thus, until the Michigan Supreme Court decides a case involving the duty owed by an independent insurance agent, the law in this State will remain in a state of flux.

Separately, Michigan law has for some time accepted the principle that a plaintiff states a cause of action in tort by alleging a loss resulting from an insurance agent's failure to procure insurance coverage as requested by the insured. *Khalaf v Bankers & Shippers Insurance Company*, 404 Mich 134 (1978). Thus, where an independent insurance agent negligently fails to procure a specific coverage requested by the insured, a cause of action will lie against the agent.

CASE STUDIES

1. In the matter of Jones Recycling.

This case involved a recycling company that moved into a large industrial building. The agent and the insured had a relationship going back roughly four years. Over the course of time, the insured acquired used equipment in its recycling process and when the equipment was purchased, the insured would contact the agent and advise that equipment had been purchased at a particular price. The insured had a replacement cost policy, but the agent did not inquire each time the insured called whether the equipment that had been acquired was "new" or "used." Since most of the equipment had been acquired "used," the replacement cost coverage for contents was calculated at far less than what it would have cost the insured to reacquire the property new. The agent met with the insured annually to discuss coverages and the insured failed to advise the agent that the coverages were inadequate. Subsequently, a fire destroyed the entire building and all of the contents, and the insured claimed that the contents were under-insured to the tune of $1,300,000.00.

In the above case, the question whether the *Harts* "no-duty to advise" standard applied or whether the *Genesee Foods* "fiduciary duty" standard applied was determinative of whether the agent had breached the applicable standard of care. We argued on behalf of the agent that the insured was in the best position to know what it would cost to replace specialized property that was used in the recycling process and at no point during any of the renewal processes did the insured ever object to the limits of contents coverage.

The attorney for the insured, on the other hand, argued that the agent was negligent in failing to inquire whether the property had been acquired new or used. The attorney also argued the agent failed to guarantee that the insured had adequate limits to protect the insured in the event of a total loss. In the above case, the agent could have potentially avoided the lawsuit by inquiring whether the property was acquired new or used and, if used, the agent should have had the insured provide replacement cost values for all of the property if replaced new rather than at the values that were ambiguously given each time a piece of property was acquired. Under a *Harts* standard of care test, the agent in all likelihood would have been acquitted of any negligence, but under the *Genesee Foods* standard of care test the agent likely would have been found liable for some degree of fault.

2. In the matter of Jane Doe.

This case involved an automobile accident involving a third party, Jane Doe, with an insured by the name of John Smith. Mr. Smith was insured personally and for his business through an independent insurance agency. At one point in time, Mr. Smith had a personal umbrella rider that was attached to a commercial umbrella policy that offered Mr. Smith $1,000,000.00 in umbrella coverage. Approximately seven years before the automobile accident, Mr. Smith changed his

commercial insurance coverage and lost the personal umbrella rider. The agency had extensive activity logs regarding all of the transactions between Mr. Smith and the agency, but there was no record of any alleged conversation between the agent and Mr. Smith authorizing the change in commercial insurance policies from company A to company B thereby eliminating the personal umbrella rider. The agent testified that such a conversation occurred, but it was never documented. Seven years later, Mr. Smith was involved in an automobile accident with Ms. Doe which resulted in Ms. Doe being a quadriplegic. Mr. Smith only had $300,000.00 of underlying automobile limits. Mr. Smith then made a sweetheart agreement with Ms. Doe whereby he assigned all of his rights against the agency to Ms. Doe and he also entered into a "Settlement Agreement" stating that Ms. Doe's injuries were worth $2,000,000.00. Ms. Doe then pursued the assignment claim against the agency for $1,700,000.00.

The two issues involved in this case were the agent's failure to record in the file material the alleged conversation with the insured authorizing the deletion of the personal umbrella rider. The second issue was whether the agency had a duty some time after the personal umbrella rider was dropped to advise the insured that a personal umbrella policy was advisable in light of the fact that the insured had personal assets that appeared to exceed several million dollars.

Ms. Doe's attorney retained an expert witness who testified that the insured should have been advised on an annual basis of the advisability of a personal umbrella policy to protect his personal assets notwithstanding that he had earlier chosen to drop his personal umbrella rider. The question then became whether the agency had a duty to specifically offer a particular type of coverage, i.e., umbrella coverage, to the insured.

Once again, the applicable standard of care for the insurance agent was going to be outcome determinative. If the *Harts* "no-duty to advise" standard applied, then it was unlikely that Mr. Smith could prevail on his theory that he should have been told about the advisability of a personal umbrella policy. However, if the *Genesee Foods* standard of care applied and the agent was held to a fiduciary duty to make sure that the insured had the most comprehensive coverage to protect his needs, it was likely that the agency and the agent would not prevail on a Motion for Summary Disposition and that a jury would likely find that the agent did not adequately provide the insured with adequate coverage since the insured in this particular matter was exposed to the tune of $1,700,000.00.

Obviously, the agent could have protected himself much better by recording in the activity logs the alleged conversation with the insured where the insured agreed to drop the personal umbrella rider and following up the conversation with written confirmation that it was the insured's decision to no longer pay the higher premium for the personal umbrella policy and rider. Subsequently, the agent could have periodically advised the insured in writing that it might be prudent for the insured to reconsider buying a personal umbrella policy in order to offer an additional layer of protection for the insured's assets.

CONCLUSION

We trust that this summary of Michigan law offers some guidance as to the uncertainty that exists as to an independent insurance agent's duty to his or her insured. The bottom line is that under the existing Michigan Court of Appeals published opinions, it would be advisable to work under the assumption that an agent has a fiduciary duty to his or her insured and that it is necessary to find the most comprehensive coverage to protect all of the insured's needs at least to the extent that those needs are made known to the agent. The best way of protecting the agent whenever any question or doubt may arise is to memorialize the conversations and/or information in a written document and, where possible, have the document signed by the insured.

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