# Agents E&O Standard of Care Project

## Washington 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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## Agent Duties in Washington

In Washington, an agent has the general duty to procure the coverage requested by a customer. *Hellbaum v. Burwell and Morford*, 1 Wn. App. 694, 463 P.2d 225 (1969). If the agent does not procure the requested coverage, he must notify the customer so that the coverage can be obtained elsewhere. *Bates v. Bowles White & Co*., 56 Wn.2d 374, 353 P.2d 663 (1960). The question always arises as to whether the agent also has a duty to investigate, discover and advise the customer as to coverages. The court in *American States Ins. Co. v. Breesnee*, 49 Wn. App. 642, 745 P.2d 518 (1987), held that in general, a customer has a duty to give his insurance agent "clear, explicit, and positive" instructions regarding the type and scope of coverage requested. If the customer's instructions are "ambiguous or obscure, and will bear different interpretations, the agent is justified in acting in good faith upon one of two reasonable constructions."

In *American States*, Breesnee owned a car lot. His son bought a Trans Am in his own name. Breesnee notified his insurance agent that he wanted the Trans Am added to his commercial car lot policy. He did not tell the agent that the car was in his son's name. The son wrecked the car and coverage was denied because the son was not a named insured and the Trans Am was not a covered vehicle under the terms of the car lot's commercial policy.

Breesnee argued that the insurance agent had a duty to make inquiries of him to determine the extent and type of coverage required. The court rejected this argument and concluded that the insured had a duty to specifically tell the agent that he wanted special coverage for a car that was not registered in the name of the car lot. The court explained that an agent does not have a duty "to make further inquiries of the person who placed the insurance order to determine the nature and scope of the insurance required."

The Washington courts have held that there is a duty to advise when there is a special relationship. A special relationship may arise under two circumstances: first, if an agent holds himself out as an insurance specialist and receives compensation for consultation and advice a part from the premium paid by the customer; or, second, if there is a long-standing relationship and some type of interaction on the question of coverage coupled with the customer's reliance on the expertise of the insurance agent to the customer's detriment. For several years, the Washington courts discussed special relationships but did not find one to exist in the cases considered by the Washington courts. *See Suter v. Virgil R. Lee & Son, Inc*., 51 Wn. App 524, 754 P.2d 155 (1988).

In *Suter*, plaintiffs did not have sufficient liability insurance to cover an auto accident and argued that an agent has a duty to recommend adequate liability policy limits. The plaintiffs presented the affidavit of an "insurance expert" who testified that an insurance agent had a duty to inquire into an insured's assets, income, occupation and real estate holdings and to recommend liability coverage adequate to protect the assets.

The court rejected plaintiff's argument and concluded "the general duty of reasonable care which an insurance agent owes his client does not include the obligation to procure a policy affording the client complete liability protection." The court also held that there was no special relationship obligating the agent to give advice because the plaintiffs had never asked anyone from the insurance agency about the adequacy of their coverages and the agency had never given them any advice in that regard. *See also Shows v. Pemberton*, 73 Wn. App. 107, 868 P.2d 164 (1994) (insurance agent not obligated to advise insured about policy coverages when there had been no request for advice); *Gates v. Logan*, 71 Wn. App. 673, 862 P.2d 134 (1993) (insurance agent had no duty to advise insured to get higher limits when agent did not procure all client's insurance); *Lipscomb v. Farmers Ins. Co*., 142 Wn. App. 20, 174 P.3d 1182 (2007) (special relationship did not exist because there was not sufficient interaction on coverage and no reliance on the agent's advice.); *American Commerce Ins. Co. v. Ensley*, 153 Wn. App. 31, 220 P.3d 215 (2009) (multi-year relationship not enough to create a special relationship); *McClammy v. Cole*, 158 Wn. App. 769, 243 P.3d 932 (2010) (no special relationship or duty to advise when agent did not give advice on the adequacy of coverage.)

In 2003, a case involving bad facts finally led to the Washington courts finding a duty to advise. *See AAS-DMP Mgmt., L.P. Liquidating Trust v. Accordia Northwest*, *Inc*., 115 Wn. App. 833, 63 P.3d 860 (2003). Accordia had been AAS's broker for 10 to 15 years. It collected a fee in addition to its commission. Accordia prepared an 80 page summary and did not give AAS the policy. Accordia also told AAS that there was no deadline on submitting claims when the policy contained a 2 year suit deadline. AAS submitted a large claim two years after the loss and the insurance carrier denied coverage. AAS could not sue the carrier because the suit deadline had expired. Not surprisingly, the court concluded that there was a special relationship and that Accordia had been negligent when it advised that there was no deadline for submitting the claim. *See also Shah v. Allstate Ins. Co.*, 130 Wn. App. 74, 121 P.3d 1204 (2005) (court found duty to advise when agent had procured insurance for years, calculated the replacement cost using the wrong square footage and represented that the policy provided replacement cost coverage); *Peterson v. Big Bend Ins. Agency, Inc.*, 150 Wn. App. 504, 202 P.3d 372 (2009) (court found violation of duty when agent promised to use Boeckh guide, used it incorrectly and misrepresented that the policy limits were determined by the cost guide).

**Case Study I**

A. Line of coverage involved: Contractors discontinued operations policy.

B. Position of person in the agency involved: Broker.

C. Personal or commercial lines: Commercial.

D. Type of coverage involved: Ongoing operations.

E. Procedural or knowledge-based error: Knowledge.

F. Claimant allegation: Broker failed to confirm that ongoing operations would roll into discontinued operations coverage.

G. Settlement or trial: Settlement.

H. Description of alleged error: Broker failed to compare marketing policy materials to actual policy issued.

I. Tip to avoid claim: Always compare quote materials to actual policy.

J. Summary of case. In the late 1990s, a California broker developed an idea for discontinued operations coverage for construction companies. The policies would provide coverage for buildings that had been completed and sold. The California broker approached a London broker who went to a Lloyd's syndicate to draft the policy. Lloyd's attorneys drafted the policy form. The initial 1998 version of the policy did not have an ongoing operations exclusion. Binders were issued for policies under the 1998 version although the actual policies were not delivered. In 2002, Lloyd's developed a new policy form that still did not have the ongoing operations exclusion. In 2003, a third version of the policy was created with an ongoing operations exclusion. The exclusion provided that there would be no coverage if the units under construction were being worked on or were owned at the time of the discontinued operations policy inception. It was not until 2003, that Lloyds finally starting issuing policies for the coverage that had been bound beginning in 1998. All the policies used the 2003 policy form. No one was told about the change in forms.

In February 2003, the Washington broker submitted an application which included two construction projects that were ongoing. The broker was provided a sample policy to review. The sample policy was the 2002 version, which did not have the ongoing operations exclusion. The broker ordered the policy believing that the two ongoing

projects would be covered once they were completed. The policy arrived six months later and the policy forms were not reviewed. The projects which were ongoing were then completed and sold. There was a later construction defect claim and Lloyd's denied coverage because the projects were ongoing and owned at the time of policy inception.

There was clearly a special relationship and the broker was obligated to give accurate advice. The broker had to concede that the contractor relied on his advice in procuring the policy. The broker also acknowledged that if he had reviewed the policy forms upon receipt of the policy, he would have known that the policy would not provide coverage for the projects which were owned and under construction at policy inception. The case was settled with contributions by the California broker, Lloyd's and the retail broker. The lesson is to completely review declaration pages and policy forms to document that they are consistent with marketing materials.

**Case Study II**

A. Line of coverage involved: D & O claims made and reported policy.

B. Position of person in the agency involved: Agent.

C. Personal or commercial lines: Commercial.

D. Type of coverage involved: D & O claims made and reported policy.

E. Procedural or knowledge-based error: Procedural.

F. Claimant allegation: Agent did not properly report claim.

G. Settlement or trial: Dismissed on summary judgment.

H. Description of alleged error: Agent reported claim to underwriter and not claims department.

I. Tip to avoid claim: Report claims to claims address in policy.

J. Summary of case. An Alaskan Native Corporation purchased a Royal D & O policy. The policy was a claims made and reported policy. During the policy midterm, new agent took over on a broker of record letter. The new agent had an agency contract with Royal. Royal sold the D & O business to St. Paul in early 2003. All underwriters and claims professionals moved from Royal to St. Paul.

On June 9, 2003, the agent was provided with a claim letter against the Alaskan Native Corporation. On June 12, 2003, the agent sent the claim letter to the St. Paul underwriter (who was the same underwriter on the prior Royal policy). The Royal D & O policy required that a claim be reported to the claims Department. The agent's procedural manual also stated that all claims should be reported to addresses identified in the policy. St. Paul issued a new policy effective June 14, 2003, and the underwriter did not forward the claim letter to the claims Department.

On October 20, 2003, the agent asked the underwriter about the status of the claim. The underwriter told the agent to submit the claim to the claims department. Nine months later, in August 2004, the directors of the Alaskan Native Corporation were sued for $8 million. Royal denied the claim, stating that there was late notice because the claim was not turned in to the claims department prior to the termination of the Royal policy on June 14, 2003.

The directors filed a lawsuit against Royal and the agent for the lack of coverage. Royal maintained that the agent was not Royal's agent for reporting of claims and that notice to the agent was not notice to Royal. Royal asserted that its agency agreement with the agent did not apply because the agent did not place the policy but instead took it over on a broker of record letter. Royal eventually settled the claims and then filed a claim against the agent alleging that the agent was negligent by not promptly reporting the claim to the claims department.

The Court dismissed Royal's claims against the agent. It confirmed that the agent was Royal's agent even though it took over the policy mid-term. The court explained that the agent's action in only reporting the claim to the underwriter was not the proximate cause of Royal having to pay the claim because if the claim had been reported prior to termination of the Royal policy, Royal would have paid the claim.

The claim against the agent could have easily been avoided if the agent would have simply followed its own procedures and reported the claim to the address identified in the policy.

**Case Study III**

A. Line of coverage involved: Commercial, mining coverage.

B. Position of person in the agency involved: Agent.

C. Personal or commercial lines: Commercial.

D. Type of coverage involved: Underground property coverage.

E. Procedural or knowledge-based error: Knowledge.

F. Claimant allegation: Agent failed to advise regarding lack of underground coverage for property.

G. Settlement or trial: Dismissed on summary judgment.

H. Description of alleged error: Agent failed to advise regarding lack of underground coverage for property.

I. Tip to avoid claim: Send letters and summaries documenting reductions in coverage. Agent should also seriously consider not working with owners who are significantly underinsuring assets.

J. Summary of case. A surface coal mine and production buildings were constructed at a cost of $3.2 million. Initially, the owners insured all of the buildings and equipment. The mine began to have financial difficulties. Gradually, over the years, the coverage was reduced to the point that the owners only covered certain buildings. A lightning strike damaged a transformer. Underground cables from the transformer to the buildings were also damaged. The policy did not provide coverage for underground cables. The owners alleged that they had lost the opportunity to reopen or sell the mine with millions in damages.

The court dismissed the agent on summary judgment. The court held that the owners had a duty to specifically request coverage for underground cables, and that the agent did not have a duty to advise regarding the lack of coverage because all coverages had been significantly reduced over the years. In particular, the owners could not show that they would have procured underground coverage for the cables when the owners were not insuring numerous other assets.

The claim could have been avoided if the agent had recommended that the owners procure their insurance elsewhere when it was obvious that the owners were significantly underinsuring the assets. It would also have been helpful if the summaries or cover letters specifically outlined the reduction in coverage.