Agents E&O Standard of Care Project

Wisconsin 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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DUTIES OF WISCONSIN INSURANCE AGENTS AND BROKERS

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I. INTRODUCTION

When purchasing insurance, the public generally looks to their insurance agent for advice on coverages and limits. When a dispute involving an uninsured loss occurs, many are surprised to discover that Wisconsin law is not always consistent with these expectations.

In a standard agent-customer relationship, Wisconsin-licensed insurance agents have no duty, absent a statutory requirement or special circumstances, to advise clients as to insurance coverages and limits. Wisconsin courts do not consider insurance agents to be financial advisors, and insureds are deemed to be in charge of their own financial affairs, including insurance needs.

However, Wisconsin-licensed insurance agents do have a duty to use reasonable diligence to obtain insurance where there is a request for coverage and an agreement to procure it.

II. DEFINITIONS OF INSURANCE AGENT AND BROKER

A. Statutory Definition: "Broker" Represents Insured

Whether an insurance salesperson is labeled a "broker" or "agent" can be important in triggering legal duties, with a greater duty owed to the entity which the broker or agent represents. The problem in assigning a label is that the courts, industry and public use the terms interchangeably, in a dual sense, and often use the term "agent" to describe just about everyone involved in insurance sales.

This problem is caused by the fact that Wisconsin statutory law and case (common) law differ on these definitions.

Under Wisconsin statutes, an insurance marketing intermediary dealing with a member of the public is, contrary to common usage, actually defined as a "broker" for most purposes. Wis. Stat. § 628.02(3) provides:

(3) Insurance broker. An intermediary is an insurance broker if the intermediary

> acts in the procuring of insurance *on behalf of an applicant for insurance or an insured*, and does not act on behalf of the insurer except by collecting premiums or performing other ministerial acts. (Emphasis added).
>
> (4) Insurance agent. An intermediary is an insurance agent if the intermediary acts as an intermediary other than as a broker.

Under the Wisconsin statutory scheme, *a Broker represents the Insured; and an Agent represents everyone else, including the Insurer*. An easy way to remember this is that an Agent usually has an Agency Agreement with the insurer, and thus an agent represents the insurer.

There are numerous Wisconsin insurance statutes confirming the premise that an agent is a representative of the insurer. For example, Wis. Stat. § 631.09(3) provides that notice to an authorized *agent* constitutes notice to the insurer; § 628.11 talks about insurance companies appointing its *agents*; and § 628.34 prohibits unfair marketing practices by *agents* of the insurer.

B. Wisconsin Case Law: "Agent" Represents Insurance Company

As noted, Wisconsin courts do not always adhere to statutory definitions, but use common business terminology. A leading modern case on Wisconsin insurance agent duty, *Nelson v. Davidson*, 155 Wis. 2d 674, 456 N.W.2d 343 (1990), discusses an "agent" in terms of a representative of the policyholder, contrary to the above-cited statutory definition:

> "[t]he mere allegation that a client relied upon an *agent* . . . is insufficient to imply the existence of a duty to advise. The principal-agent relationship cannot be so drastically expanded unilaterally."

Id., 155 Wis. 2d at 684 (emphasis added).

Wisconsin courts have also recognized that agents and brokers often operate in a dual capacity, sometimes as a broker on behalf of their customer, and sometimes as an agent on behalf of their insurer.

In the significant Wisconsin case of *Appleton Chinese Food Service, Inc. v. Murken Insurance, Inc.*, 185 Wis. 2d 791, 805, 519 N.W.2d 674 (Ct. App. 1994), the Wisconsin court of appeals stated that the insurance broker becomes an agent of the insured for purposes of selecting a company. The court referred to this as a dual agency, noting that "[t]he concept of dual agency is familiar to Wisconsin and the insurance industry." *Id.* at 806, quoting with approval 16 Appleman, Insurance Law & Practice, § 8736 (1981) ("It is not unusual for an insurance agency to represent both insurer and insured.").

The Wisconsin statutory scheme, dual capacity doctrine, and common business and legal terminology relating to "agents" and "brokers" can lead to confusion. The key is to examine the

activity of the agent at any given time in the process of procuring and maintaining an insurance policy. This will usually determine whom the insurance intermediary represents and, thus, to whom a duty is owed.

As discussed below, however, a statutory insurance broker who is asked to procure coverage and agrees to do so becomes an agent of the insured for purposes of carrying out the request.

III. STANDARD OF CARE OF AGENTS AND BROKERS

A. General Rule: Coverage Request and Agreement to Procure Required to Create Duty

In 1990, the Wisconsin supreme court issued a major decision protecting insurance agents from liability in ordinary agent-customer relationships. The case, *Nelson v. Davidson*, 155 Wis. 2d 674, 684, 456 N.W.2d 343 (1990), involved a claim that an insurance agent had a duty to inform its customer that underinsured motorist (UIM) coverage was available. The Wisconsin supreme court held as follows:

> "[A]n insurance agent has no affirmative duty, absent special circumstances, to inform an insured concerning the availability or advisability of UIM coverage."

Id., 155 Wis. 2d at 685.

The *Nelson* decision set the stage for a series of pro-agent court decisions holding that an agent has no duty to advise as to coverages. See, e.g., *Meyer v. Norgaard,* 160 Wis. 2d 794, 802, 467 N.W.2d 141 (Ct. App. 1991) (agent had no duty to offer greater limit than statutory UM limit); *Tackes v. Milwaukee Carpenters District Council Health Fund,* 164 Wis. 2d 707, 717, 476 N.W.2d 311 (Ct. App. 1991) (no duty to offer UIM coverage, which was non-mandatory at the time; mere fact that agent recommended coverages did not transform relationship into special circumstances relationship); *Lenz Sales & Service, Inc. v. Wilson,* 175 Wis. 2d 249, 257, 499 N.W.2d 229 (Ct. App. 1993) (no duty to advise of adequacy of replacement cost coverage limit).

The *Nelson* holding quickly made its way into the Wisconsin jury instruction on insurance agent duty, Wis. JI – Civil 1023.6, which provides, in pertinent part:

> Negligence Of Insurance Agent
>
> An insurance agent must use the degree of care, skill, and judgment which is usually exercised under the same or similar circumstances by insurance agents licensed to sell insurance in Wisconsin.
>
> While there is no duty to advise the policy holder of coverages available, the agent

> must use reasonable skill and diligence to put into effect the insurance coverage requested by his or her policy holder, act in good faith towards that policy holder, and inform him or her of the minimum statutory requirements. A failure on the agent's part to use that skill or diligence constitutes negligence.

This jury instruction is a powerful tool in defending against claims by insureds that an agent failed to advise or inform as to insurance coverages.

It has been argued that the *Nelson* rule is inconsistent with Wis. Stat. § 628.02(1), which defines an agent as a person who advises someone about their insurance needs. While this statute recognizes that, for definitional purposes, an insurance agent is one who advises, the courts have made clear that there is no legal duty to do so. For example, the Wisconsin court of appeals held in the *Tackes* case, cited above, that the mere fact that an agent offers advice does not create a duty to do so. *Id.*, 164 Wis. 2d at 716-17.

Wisconsin courts have also made clear that a broker must agree to procure coverage before any duty to do so arises. When an insurance agent fails to act with reasonable care, skill, and diligence in procuring coverage he or she agreed to procure, the agent has breached his or her duty to the insured. *Appleton Chinese Food Service, Inc. v. Murken Insurance, Inc.*, 185 Wis. 2d 791, 805, 519 N.W.2d 674 (Ct. App. 1994).

This rule was more recently reaffirmed the Wisconsin supreme court in *Avery v. Diedrich*, 2007 WI 80, 301 Wis. 2d 693, 734 N.W.2d 159, 164, in which the court stated:

> We hold that an insurance agent does not have a duty to procure requested insurance coverage until there is an agreement that the agent will do so.

Id., 301 Wis. 2d at 697, 2007 WI 80, ¶ 2.

The *Avery* court distinguished the *Appleton Chinese Food* case as follows:

> Contrary to the Averys' suggestion, the *Appleton Chinese* insurance agent breached her duty because of her negligence *after she had agreed to procure the requested coverage*. *Appleton Chinese*, 185 Wis. 2d at 805.

Id., 301 Wis. 2d at 708, 2007 WI 80, ¶ 33 (emphasis added).

Moreover, the request for coverage must be fairly specific. An agent is ordinarily not liable where an insured makes a general request for the "best available coverage." Wisconsin courts consider such a request to be subjective. *Meyer v. Norgaard,* 160 Wis. 2d 794, 802, 467 N.W.2d 141 (1991).

B. Examples Triggering or Negating Agent Duty

1. Lapsed Coverage. A common scenario facing agents is a slow-pay or late-pay account. Most insurers send direct notices of cancellation or lapse to the insured in this situation. The question arises as to whether the agent has a duty to take any action to prevent a lapse or cancellation, such as reminding the insured to pay the overdue premium.

No Wisconsin cases address this specifically, but general case law indicating that an agent has no duty to advise as to available coverages would strongly suggest that an agent has no responsibility to "chase" an insured to pay its premiums.

However, where the agent has routinely reminded the insured to pay overdue premiums, or paid premiums to the carrier on the insured's behalf, a so-called "special relationship" may be created, giving rise to a duty. See sec. III.B.5., below.

2. Obsolete Coverage Limits. In *Lisa's Style Shop, Inc. v. Hagen Insurance Agency, Inc.*, 181 Wis. 2d 565, 577, 511 N.W.2d 849 (1994), the Wisconsin supreme court held that the agent did not have a duty to increase insurance for store inventory where the insured did not ask for increased limits and the agent did not agree to obtain it. However, the agent did have a duty to maintain the existing insurance.

Insurance agents do not have a duty to inform about or recommend policy limits higher than those selected by the insured, *Meyer*, 160 Wis. 2d at 798, or to update the contents limit of the policy or to advise them regarding the adequacy of coverage. *Lenz Sales & Service, Inc.*, 175 Wis. 2d at 255.

3. Explaining Exclusions to Insured. An agent may have a duty to alert the insured to an exclusion that will nullify the coverage the insured is requesting, if the agent is made aware of facts that would trigger the exclusion. In *Poluk v. J.N. Manson Agency, Inc.*, 2002 WI App 286, 258 Wis. 2d 725, 653 N.W.2d 905, the Wisconsin court of appeals held that where an agent is told that a rental property will be vacated, there is a duty to advise the insured of a vacancy exclusion. This case was distinguished from other cases finding no duty, on the ground that the agent knew the insured was in effect requesting continuing coverage and therefore should have been advised of the vacancy exclusion. *Id.*, 258 Wis. 2d at 736.

4. Statute or Ordinance Mandating Coverage. In *Mercado v. Mitchell*, 83 Wis. 2d 17, 264 N.W.2d 532 (1978), a carnival ride operator was required by city ordinance to have liabilility insurance in place and indicated to the agent that a certificate of insurance was required to be filed with the municipality. This triggered a duty on the part of the agent to procure the mandatory coverage. *Id.*, 83 Wis. 2d at 29.

5. Special Circumstances Trigger Duty to Advise. As noted, Wisconsin courts distinguish a "special relationship" from a "standard insured-insurer relationship." Where there is a special relationship, the agent has a duty to advise the client as to coverages.

Examples of a special relationship are: an express agreement that an agent will advise the insured about coverage; payment of compensation over and above the agent's standard commission; a long-standing pattern of entrustment from which it appears that the agent appreciated a duty to advise; and the agent representing iself as highly skilled and the insured relying on this. *Nelson v. Davidson,* 155 Wis. 2d 674, 683-84, 456 N.W.2d 343 (1990).

6. Insurance Binders. An insurance binder is a temporary insurance contract generally used to prove the existence of a policy of insurance. It is usually followed by a formal insurance contract.

A binder remains in force until cancelled or a written insurance policy is issued. The terms of the binder track with the terms of the policy described therein. *Gross v. Lloyds of London Insurance Co.*, 121 Wis. 2d 78, 89, 358 N.W.2d 266 (1984).

Wisconsin statutes recognize oral binders. Wis. Stat. § 631.05 provides as follows:

> Oral contracts of insurance and binders. No provision of chs. 600 to 646 and 655 may be interpreted to forbid an oral contract of insurance or issuance of a written binder. The insurer shall issue a policy as soon as reasonably possible after issuance of any binder or negotiation of an oral contract.

It is not uncommon for an agent to orally bind coverage, pursuant to binding authority set forth in the insurer's underwriting guidelines, or a specific grant of authority received from the insurer. Most agents have specific disclaimers in voicemail greetings that coverage cannot be bound by recorded voicemail messages.

Once a binder is issued, the insurer has 60 days cancel it, and must give a 10 days' notice. Wis. Stat. § 631.36(2)(c). Thus, the carrier has time to underwrite the bound risk and determine whether it wants to issue a formal policy.

If an agent issues a binder without authority, the insurer must cover any loss that occurs while the binder is in effect, but then has a right to sue the agent for indemnification. *Schurmann v. Neau*, 2001 WI App 4, ¶ 9, 240 Wis. 2d 719, 726, 624 N.W.2d 157.

7. Electronic Applications and Signatures.

Most insurance agents process quotes and applications electronically, typically by using a web site maintained by the insurer. Under Wis. Stat. § 137.15:

> (1) A record or signature may not be denied legal effect or enforceability solely because it is in electronic form.
> (2) A contract may not be denied legal effect or enforceability solely because an electronic record was used in its formation.

(3) If a law requires a record to be in writing, an electronic record satisfies that requirement in that law.
(4) If a law requires a signature, an electronic signature satisfies that requirement in that law.

The recognition of electronic contracts and signatures has been in effect in Wisconsin since 2004, but some Wisconsin Insurance statutes have not expressly incorporated the concept. For example, Wis. Stat. § 631.11(4)(a) protects an insurer from being deemed to have the same knowledge its agent has regarding a misrepresentation by the applicant for insurance:

(4) Effect of insurer's knowledge.

> (a) Knowledge when policy issued. No misrepresentation made by or on behalf of a policyholder and no breach of an affirmative warranty or failure of a condition constitutes grounds for rescission of, or affects an insurer's obligations under, an insurance policy if at the time the policy is issued the insurer has either constructive knowledge of the facts under s. 631.09 (1) or actual knowledge. *If the application is in the handwriting of the applicant,* the insurer does not have constructive knowledge under s. 631.09 (1) merely because of the agent's knowledge. (Emphasis added).

Since this statute talks about the applicant's handwriting, it is unclear whether an electronic application counts. Insurance applications or submissions are now often done online by the agent using the carrier's website, and the insured will not even fill out or sign an application.

The Wisconsin court of appeals construed § 631.11 in *Smith v. Dodgeville Mut. Ins. Co.*, 568 N.W.2d 31, 35-36 (Ct. App. 1997) and found a "legislative intent to compel an incorporation of the actual statements made by the applicant who has become an insured under the policy at issue." Again, applications are often completed by the agent or a customer service agent online, based on telephone discussions with the insured. The electronic transactions statute cited above notwithstanding, it is unclear whether an electronic submission will satisfy the requirements of § 631.11.

The best practice in this situation is to obtain an actual signature on new accounts, using the electronic application process for subsequent renewals.

IV. CAUSATION: AGENT NOT LIABLE IF CONDUCT DID NOT CAUSE LOSS

It is not unusual for an agent's error to be non-causal. An insured may attempt to sue an agent for negligently failing to procure a particular endorsement, only to have the carrier deny coverage under that endorsement. Thus, even had the requested coverage been procured, it

would not have covered the loss, and the negligence was non-causal.

The same rule applies in cases in which an insurer sues its agent for negligently failing to process a coverage request for which the insurer was forced to make a loss payment. If the insurer would have accepted the risk anyway, there is no causal link between the agent's negligence and the carrier's loss payment. As the Wisconsin court of appeals stated in *Peterman v. Midwestern Nat'l Ins. Co.*, 177 Wis. 2d 682, 503 N.W.2d 312, 321-22 (Ct. App. 1993)

> . . . where the alleged negligence of the agent does not alter the risk accepted by the insurer, or the insurer normally accepts such risks in the normal course of business, the agent's negligence *is not the cause* of the loss and the agent is not liable therefore.

Id., 177 Wis. 2d at 705.

V. DAMAGES RECOVERABLE BY INSUREDS AND INSURERS AGAINST AGENTS

A. Insured Has Right to Elect to Sue Agent or Carrier, or Both

In a case involving disputed coverage, an insured has the choice of suing the agent for failing to procure the coverage, or the insurance company on the policy itself. *Hause v. Schesel,* 42 Wis. 2d 628, 167 N.W.2d 421 (1969). An insured can also sue both the agent for negligence or breach of contract, and the insurer for reformation of contract. *Scheideler v. Smith & Associates*, 206 Wis. 2d 480, 486-87, 557 N.W.2d 445 (Ct. App. 1996).

Eventually, the insured must elect which remedy and party it wishes to pursue or to pursue partial recovery from both. The insured cannot obtain a double recovery from both the insurer and agent. *Id.*, 206 Wis. 2d at 487. If an insured settles for only a portion of its loss from either the agent or carrier, there is still an intact claim for the balance against the non-settling party. *Appleton Chinese Food Service, Inc.*, 185 Wis. 2d at 807-08.

Where the insurer settles the entire claim with its policyholder and then attempts to pursue a claim against the agent *under an assignment of the policyholder's claim*, the claim is barred under the election of remedies doctrine because, once the insured elects its remedy and recovers from the insurer, it no longer has any claim to assign. *Scheideler v. Smith & Associates*,, 206 Wis. 2d at 489.

However, this pitfall can be avoided if the party making the full payment pursues the other party directly under the agency agreement, instead of indirectly, under an assignment. For example, where the agent settles the entire claim with the insured and sues the insurer *under the agency agreement,* the election or remedies doctrine does not bar the claim. *Artisan & Truckers Cas. Co. v. Thorson*, 2012 WI App 17, 339 Wis. 2d 346, 359, 810 N.W.2d 825.

B. Reformation

Reformation is an equitable claim to "reform" an insurance policy which, because of a mistake, does not reflect the intentions of the parties. *Trible v. Tower Ins. Co.,* 43 Wis. 2d 172, 182, 168 N.W.2d 148, 154 (1969). The insurance policy is essentially rewritten by the court, or "reformed," to reflect the parties' intentions.

If the policy is reformed, the insurer does not have the right to recover its loss payment from the agent because, if requested, the insurer would have issued the policy. *Peterman v.Midwestern Nat'l Ins. Co.*, 177 Wis. 2d 682, 705, 503 N.W.2d 312 (Ct. App. 1993). The only right of recovery the insurer would have against the agent would be for the premium. *Scheideler v. Smith & Associates,* 206 Wis. 2d 480, 490 fn. 5, 557 N.W.2d 445 (Ct. App. 1996).

There does not appear to be any Wisconsin case law authorizing an agent to pursue a reformation claim against an insurer. A reformation claim is essentially a dispute between the parties to an insurance contract, so arguably the claim belongs only to the insured.

C. Measure of Damages in Agent Negligence Cases

Damages available to the insured because of an agent's failure to procure are measured by whatever policy benefits would have been paid had coverage been procured. *Wagner v. Falbe & Co.,* 272 Wis. 25, 27-28, 74 N.W.2d 742, 744 (1956).

Similarly, damages available to the carrier when an agent negligently binds it to an unacceptable risk consist of the indemnity payment made by the insurer. *Appleton Chinese Food v. Murken Ins.*, 185 Wis. 2d at 808.

VI. CASE STUDIES OF AGENT CONDUCT

A. Crane Operator Asks to Duplicate Non-renewed Coverage

The agency client, a crane operator, had coverage through Carrier A, which non-renewed the policy.

Rather than simply asking for another policy to replace the non-renewed policy, the client transferred its cranes and crane operation to a related business entity which had insurance through Carrier B.

The agent admitted that the client asked to duplicate its non-renewed coverage on the crane operation by using the business transfer maneuver. However, Carrier B would not insure the transferred crane because it was not being operated by an employee of the agency client at the time of the loss.

Result: Even though the agent failed to obtain replacement insurance on the crane, it was of no consequence since the carrier denied coverage anyway. Hence, there was no causation.

B. Liquor Store Owner Claims CGL Policy Covers Liquor Liability

Agency client, a liquor store, sold alcohol to a minor, who caused injury while driving drunk.

The agency client had purchased a standard commercial general liability policy, which clearly excluded coverage for claims relating to sale of alcohol to minors. However, the client claimed that he understood that the liability policy would cover all types of liability, even sale of alcohol to minors. He admitted he did not specifically ask for the coverage.

Result: This was a classic case of no duty arising on the part of the agent since there was no coverage request, and no agreement to obtain the disputed coverage. The case against the agency was eventually dropped.

C. Agent Attempts to Pursue Insured's Claim for Reformation of Homeowners Policy

Agency client incurred a loss due to basement drain backup, and sought to recover under a homeowners policy.

An earlier homeowners policy had included an endorsement for losses due to sewer backup, and would have covered here. But the current homeowners policy did not contain that endorsement, so the carrier denied coverage.

The agent admitted that he intended to duplicate the earlier policy, and through clerical error, had failed to request the endorsement in question. The agent paid the homeowners loss and received an assignment of the insured's claim to reform the policy.

Reformation would have been available to the insured because the homeowner's policy did not reflect the intentions of the parties in that it did no include the sewer backup endorsement.

Held: The insured elected its remedy be settling its entire claim with the agent, and it had no claim to assign to the agent. Therefore, the agent was not allowed to sue the carrier for reformation.

D. Client Vacates Home – Builds New One Next to It

Agency client built a new home next to the old one, and retained the same mailing address. The client moved into the new residence, and the existing homeowners policy was then

renewed using the same address, on the same terms.

The client stored furniture and other belongings in the old house, but lived in the new house. Utilities at the old house were discontinued.

A fire loss occurred to the old house two years after it was vacated.

Held: Insured did not request coverage on new house, which was larger and would have required a more extensive policy. Therefore, the agent had no duty to inquire or advise the insured to obtain a new homeowners policy.

Caveat: Had the agent been made aware of the vacancy, there likely would have been a duty created, under the *Poluk* case cited in sec. III.B.3., above.

VII. SUMMARY

Wisconsin law is fairly favorable to insurance agents, imposing a duty to procure insurance only if there is an agreement to do so. There is no duty to advise an insured as to coverages except in relatively rare cases involving a special, non-conventional relationship between the agent and client.

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