The Insured vs. Insured Balance

In the legal world it's often said that a lawyer who represents himself has a fool for a client. While an insurance agent who places his own policy might not be considered a fool, it may create some coverage issues under his errors and omissions policy.

Like many other policies, most E&O policies contain an insured vs. insured exclusion. Generally, the exclusion states that the policy does not cover claims or disputes between insureds under the policy. For example, an agent fails to place coverage for his own property and a claim is made against the agency for failure to obtain the coverage. In that situation, if there was no insured vs. insured exclusion, the E&O policy would then become the property policy that the agent should have procured. This situation creates a potential moral hazard on the part of the agent. Why should he care if he has adequate coverage (or any coverage at all) if he has an E&O policy which would take effect? That's obviously not the purpose of an E&O policy, and the rating and underwriting of the E&O policy does not contemplate such an exposure.

E&O carriers recognize that there are situations where insurance coverage is provided from one insured to another in the agency as part of the normal professional services of an insurance agency and should be covered. Generally this includes wrongful acts arising from professional services performed by an insured who is the client, provided that the insured rendering the professional services does not own an equity interest in the property to be insured.

Most E&O policies also define the ownership interest an insured must have in an enterprise that qualifies a transaction for the insured vs. insured exclusion. Typically, this is an equity interest of 10% or more but may exclude a claim by the enterprise if an insured operates, controls or manages that entity. Say an agent places property coverage for an apartment building owned by a company in which it is a 25% partner. If there's a fire loss and the building is found to be underinsured, and a co-insurance penalty is assessed, the entity would then make a claim against itself for failing to have the building adequately insured. Again this creates a moral hazard as the enterprise that was partially owned by the insured would never have any exposure unless the E&O policy limits were inadequate, and it would never have to make sure that the limits for his property coverage were adequate. This is not the sort of risk that an insurance carrier is looking to accept.

Clearly, most agents aren't looking to deceive the E&O carrier, but they should be aware that there may be situations in which they could unintentionally be subject to the insured vs. insured exclusion. The agent or agency needs to understand that there are situations in which the definition of a professional service or what constitutes an insured vs. insured claim is not so clear, especially when dealing with non-traditional types of coverage. What if the agent also serves on the board of a not-for-profit entity while at the same time placing coverage for that entity? What if the agent is the president or CEO of the not-for-profit? It's possible that this could meet the exclusion language of "operate, control or manage."

It is possible for an agency insured to provide professional services to another insured client and still have coverage for any resulting wrongful acts that arise out of such services. However, an insured cannot obtain coverage for himself. In addition, if an insured does provide professional services to another insured, he cannot do so if he has more than 10% equity interest or operates, controls or manages 10% or more of that which is being insured.

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