

Life Lines

How to handle E&O claims about life insurance

By David Holt

Who among us hasn't learned the hard way that many tasks look easy when you've never tried them?

On the surface, it seems like dabbling in procuring a life insurance policy for a good customer would present little risk for an errors & omissions claim. But in reality, seemingly foolproof steps can result in a claim against even the most experienced insurance agent in several common ways



Material nondisclosure: The most frequent type of life insurance E&O claim arises when a client dies and the life insurer refuses to pay death benefits on the basis that the client failed to disclose material facts regarding their health history. The policy beneficiary sometimes files suit, alleging that they disclosed their health history to the agent or that the agent was negligent in the application process.

Avoid passing judgment on what an insurer wants to know about an applicant. Always err on the side of disclosure.

Contestability and suicide clauses: Sometimes a claim involves a client who already has a life insurance policy in place but decides to replace the policy to obtain increased limits or reduce premiums. That new policy contains a contestability clause providing that if the client dies within the first two years in most jurisdictions, the insurer can deny the claim for material nondisclosures as discussed above.

After two years, however, the insurer cannot deny the claim unless it can prove the material nondisclosure was due to fraud, rather than simply oversight. Similarly, the new policy will not pay if the client commits suicide within the first two years after the new policy is issued. In these cases, the beneficiary may sue the agent for failing to adequately explain the clauses.

Consider having the applicant sign a separate statement confirming their understanding that, by replacing policies, the contestability clause and suicide clause become effective again for the stated period. Alternatively, summarize those objectives in an email or other communication to the client and capture it in your system.

Cancellation for nonpayment of premium: Some life policies are canceled for nonpayment of premium, even though the policyholder had both the ability and intent to

continue paying premiums—for example, a client might not receive an invoice from the life insurer due to a change of address.

Some jurisdictions may impose a duty on the agent to make reasonable efforts to contact a client if the agent learns of a policy cancellation for nonpayment. Always keep documentation in the client's file to thwart an E&O claim of this nature, and carefully record efforts to contact the client about a cancellation.

David Holt is a vice president and claim expert at Swiss Re Corporate Solutions and works out of the Overland Park, Kansas office.

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