

## The Special Relationship and the Insurance Producer

by Stanley L. Lipshultz, JD, CPCU

### Introduction

The *special relationship* advanced in insurance agent/broker lawsuits has been recognized by courts for a long time, although lately, allegations of the existence of the special relationship have become ubiquitous, finding their way into almost every claim against the insurance agent or broker.<sup>1</sup> When properly used, the special relationship is a powerful tool in the hands of the skilled policyholder's attorney.

Plaintiffs use the special relationship to support a general duty to provide advice to a policyholder or as a separate cause of action alleging an additional legal threshold duty to provide some type of advice to the policyholder. Defendants usually counter that the special relationship simply does not exist based on the facts or, alternatively, that it places on the producer an otherwise-egregious burden of furnishing advice to clients regarding the selection of "adequate" limits or the purchase of arcane insurance coverages that might be available or somehow applicable to the risk and its exposures.<sup>2</sup>

### Special Relationship Illustrative Cases

*Bruner v. League Insurance Company* involved an agent's alleged affirmative duty to give advice as to the adequacy of coverage. The plaintiffs, Thomas and Lora Bruner, received notice from their automobile insurer that uninsured motorist coverage had been deleted from their policy but remained available upon request. Neither plaintiff contacted their agency concerning the deleted coverage. After Lora Bruner was seriously injured by a hit-and-run driver, she attempted to retroactively reinstate the uninsured motorist coverage through the use of the special relationship by alleging that the defendant agency had a duty to advise plaintiffs about the adequacy of their coverage.<sup>3</sup> The Court of Appeals of Michigan found that no question of fact existed concerning the special relationship, as plaintiffs had neither contacted the agency following the notice of the deletion of the uninsured motorist coverage nor inquired as to the nature and cost or whether to purchase the coverage.<sup>4</sup>

*Rawlings v. Fruhwirth* also involved an alleged failure of the agent to recommend coverage in an automobile policy. Plaintiff's son died as a result of injuries sustained in an automobile accident in July 1985. After settling a wrongful death suit with Charles Sweeney, the negligent driver, Rawlings took an assignment of Sweeney's rights and sued Sweeney's agents and insurer.<sup>5</sup> Using agents from two separate agencies, the insured, Sweeney, procured an automobile liability policy from one (Fruhwirth) and an umbrella liability policy from the second (Larson) but did not request Larson to procure additional liability insurance to fill the gap in limits between the existing liability policy and the umbrella.<sup>6</sup> The court rejected Sweeney's argument that a special relationship existed between Larson and Sweeney imposing on Larson a duty to procure additional insurance

**Stanley L. Lipshultz, JD, CPCU**, is a consultant and an expert witness in insurance matters. He received his JD degree in 1970 from American University Washington College of Law and earned the CPCU designation in 1989. As a practicing attorney, he defended insurance agents, brokers, and their E&O insurers for more than twenty-five years as defense counsel before retiring from the active practice of law in 1999. He has consulted in numerous matters, including agent and broker standard of care, insurance coverage, and bad faith.

not expressly requested. Even though Sweeney discussed the gap with Larson and Larson recommended that Sweeney obtain insurance to cover the gap, no request was made to Larson to procure this insurance.<sup>7</sup> Citing Bruner, *supra*, the Rawlings court agreed that the special relationship required more than the standard policyholder-insurer relationship triggering the duty to advise the policyholder about insurance coverage; and, that there must be a long-standing relationship and some kind of communication on a question of coverage with the insured relying on the expertise of the agent to the insured's detriment.<sup>8</sup>

The Court of Appeals of Arizona took a slightly different approach to the question of whether an agent has a duty to recommend or give advice as to the need for any specific insurance coverage. In the case of *Southwest Auto Painting and Body Repair, Inc. v. Binsfeld*, the court reversed and remanded for further proceedings the granting of a motion for summary judgment in favor of the agent.<sup>9</sup> The trial court had granted Binsfeld's motion holding as a matter of law that an agent has no duty to recommend or offer advice as to the need for additional coverage. Robert Lanzon, the owner of Southwest, decided to use Binsfeld's insurance agency, envisaging body shop referrals from the agency. Lanzon alleged that Binsfeld recommended certain insurance coverages and that Lanzon relied on Binsfeld and the agency for advice on the procurement as well as the appropriate coverage for the business.<sup>10</sup> Binsfeld did not discuss or mention employee dishonesty coverage, and Lanzon was unaware such coverage existed. Lanzon did not seek any advice concerning his insurance coverage from 1986 to 1989. A bookkeeper hired by Lanzon in September 1986 embezzled \$150,000 over the three-year period in question. A claim presented by Southwest was denied by the insurer due to the lack of coverage. Southwest sued its agents, alleging that the failure to offer or advise of the need for employee dishonesty coverage "fell below the standard of care expected of an insurance agent and broker who obtain insurance coverage for a business."<sup>11</sup> The agency responded that Arizona law does not recognize an additional duty to give advice unless the agent has a special relationship with the insured and that no such relationship existed. Southwest provided expert testimony that, based on those individuals who had check-signing authority, the standard of care required the agent to give advice about the availability of applicable types of coverage, particularly fidelity coverage. The trial court found that the agent's general duty did not impose an affirmative duty to offer or recommend specific insurance coverage and that there was no special relationship that might have imposed such a duty.<sup>12</sup> In its finding, the trial court completely rejected Southwest's expert's opinion. In reaching its decision, the appellate court held that an agent owes a duty to exercise reasonable care, skill, and diligence in procuring insurance coverage, even absent a special relationship, concluding that the trial court erred in finding no duty as a matter of law. The court discussed the distinction between legal duty and standard of care.<sup>13</sup> Relying on deposition testimony of Southwest's expert, the court concluded that the testimony raised a question of fact as to whether the standard of care required Binsfeld to advise as to relevant types of coverage available.

In *Trupiano v. Cincinnati Insurance Company*, the Court of Appeals of Indiana, applying Michigan law and also relying on Bruner, upheld a grant of summary judgment in favor of the agent, Alkema; his agency, SZW; and the Cincinnati Insurance Company against Trupiano. SZW and Alkema had a continuous fourteen-year relationship with Trupiano and his company, OSC, during which time Alkema "advised OSC concerning various types of business coverage, including worker's compensation, comprehensive general liability, blanket building and contents insurance, loss of business income, and fleet insurance."<sup>14</sup> Trupiano met with Alkema at least once a year to discuss insurance matters,<sup>15</sup> and SZW sent an annual letter outlining OSC's entire insurance program, including the adequacy of the recommended coverages as well as those coverages that

## Abstract

*The special relationship doctrine can create an overwhelming burden for the unsuspecting insurance agent or broker by imposing a duty to provide advice to a policyholder concerning all possible coverages and in some instances a responsibility to give advice as to what limits to purchase and whether such limits are "adequate." This article explores the nuances of the special relationship and provides a template for the producer, the policyholder, and their respective attorneys to follow by illustrating the circumstances that give rise to the special relationship between the producer and the policyholder/insured. Navigating the special relationship minefield is not an easy task, especially because actions the producer innocently perceives as being "value added" may create a legal duty where none was contemplated. Knowing the elements of the special relationship will allow the producer to decide whether embracing it—as opposed to avoiding it—will enhance the producer's connection with the client by using the special relationship to inspire a client to focus on aspects of the insurance procurement transaction that do not involve the bottom line. This article makes it clear that the special relationship is not premised on such relationship factors as longevity, social interaction, reliance for non-property and casualty advice, or even providing unsolicited advice under most circumstances.*

Alkema felt were deficient. In 1985, Trupiano purchased an automobile liability policy through Alkema with Cincinnati to insure his business fleet of seven automobiles. In December 1989, Trupiano and his wife were injured in an automobile accident and settled with the negligent driver for policy limits of \$100,000. Because Trupiano's policy contained \$40,000 uninsured/underinsured limits, they were not entitled to any benefits under their underinsured motorist coverage. The Trupianos brought an action against Alkema, SZW, and Cincinnati, alleging that the underinsured motorist limit was "wholly inadequate."<sup>16</sup> In appealing from the trial court's grant of summary judgment, Trupiano argued that there was a special relationship between Alkema/SZW and OSC/Trupiano "which would create a duty to advise about the adequacy of the insurance coverage."<sup>17</sup> The court found that the facts were insufficient to overcome Trupiano's general allegations that "Alkema and SZW held themselves out as insurance professionals and either knew or should have known that [Trupiano] and OSC were relying on them for appropriate advice on the types and amounts of business auto insurance coverage they should have."<sup>18</sup> The facts did not support any interaction between the parties on the question of uninsured/underinsured motorist coverage.

In *Murphy v. Kuhn*,<sup>19</sup> the Court of Appeals of New York rejected plaintiffs Murphy and Webster Golf Course Inc.'s argument that Kuhn was required to give advice as to possible additional insurance coverage needs based on the special relationship. Kuhn began providing property and casualty insurance to Murphy's business in 1973 and in 1977 began providing homeowners and automobile insurance to Murphy. A personal auto policy was placed for Murphy in 1990 but later in the year was in jeopardy of cancellation due to the driving records of his children. Murphy transferred the car his son used (although titled and registered in Murphy's name) to the business's commercial auto policy. The liability limits on this policy remained unchanged from 1984 through the date of an accident in 1991 involving Murphy's son. The 1991 accident involved a death and serious injuries. Murphy did not request higher liability limits for his personal and family automobile policies at any time prior to the accident. Murphy paid an additional \$200,000 over policy limits to settle the injury claims and then sued the agents for reimbursement. The thrust of Murphy's argument was "that a special relationship developed from a long, continuing course of business between plaintiffs and defendant insurance agent, generating special reliance and an affirmative duty to advise with regard to appropriate or additional coverage."<sup>20</sup> The court concluded that the plaintiffs had not established a factual basis for the special relationship. Stating that there is a "high level" necessary to recognize the special relationship threshold, "... the record . . . presents only the standard consumer-agent placement relationship, albeit over an extended period of time."<sup>21</sup>

In the case of *Peter v. Schumacher Enterprises, Inc.*, the Alaska Supreme Court addressed the question of whether insurance agents have a common law duty to give advice to their customers about their insurance coverage, concluding that such a duty exists but is dependent upon the existence of the "special relationship." The seminal issue revolved around the agent's alleged failure to advise and recommend to the insured that higher UM/UIM limits could and should be purchased after the insured asked for "full coverage." Peter alleged that Last Frontier, the agency, made no inquiries into the financial status, family needs, asset value, or importance of UM/UIM coverage in procuring a policy of automobile insurance. The agent countered that various limits were discussed and Peter was provided with written information describing levels of available UM/UIM limits. The insured, Donita Peter, also signed a document stating that she "unequivocally selected" the UM/UIM limits found in the policy. As a result of its conclusion that Donita Peter's affidavit raised genuine issues of material fact concerning the existence of a special relationship, the court reviewed a number of cases,

including *Murphy*. The court left the adequacy of coverage limits query squarely with the insured, finding that such is a matter of opinion. The court also reasoned that:

... an undesirable consequence of imposing such a duty would be that agents would defensively tend to advise their customers to buy the highest, most comprehensive and expensive coverages rather than the more modest packages that most people of similar means would find suitable. This could result in a mis-allocation of personal resources of individual insureds.<sup>22</sup>

The court remanded the matter to the trier of fact to determine whether the facts supported a finding of a special relationship. Should the special relationship be found to exist, then the next step would be to determine whether Last Frontier's advice, whether implied or obvious, was reasonable or whether higher UM/UIM limits should have been recommended.<sup>23</sup>

In *Zaremba Equipment, Inc. v. Harco National Insurance Company*, Harco appealed from a jury verdict of \$2,353,778 a portion of which included a deficiency in replacement cost limits for a building and contents of \$1,192,000. Zaremba had been insured for seventeen consecutive years with Harco. Plaintiff alleged that at some unspecified time before a total loss of its primary business premises in 2003, Jimmy Zaremba, the insured's business manager, had informed Harco's agent, Patrick Musall, that "it wanted to be fully insured so it could rebuild and replace its property in the event of a complete loss."<sup>24</sup> Plaintiff further alleged that Musall indicated Harco could issue a replacement cost policy adequate to rebuild plaintiff's building. From approximately 1998 through the 2002 renewal of the Harco policy, Musall met with Zaremba at least twice a year to discuss insurance needs, available coverages, and potential policy limits. Before accepting Harco's 2002–2003 renewal proposal, Zaremba showed Musall a proposal from a competing insurer that included, among other things, building coverage limits in the amount of \$450,000 with "Guaranteed Replacement Cost."<sup>25</sup> "Musall conceded that Jimmy had asked him to 'meet or beat' the [other] proposal and expressed a desire 'to be fully insured.'"<sup>26</sup> Musall used a Marshall & Swift software program to prepare a cost estimate for the reconstruction of the building, which was ultimately insured for \$525,000. Musall also conceded that he made specific recommendations as a result of Zaremba's request to be "fully insured."<sup>27</sup> Although the policy covering the loss had not been received prior to the fire, Zaremba admitted that he had not read any of the previous policies. On appeal, Harco challenged the jury verdict on a number of grounds, including the negligence verdict.<sup>28</sup> The defendant launched a multi-pronged attack on the negligence verdict, beginning with the insured's failure to read the policy as well as the insurance quotations provided to the plaintiff. Defendant argued that had the plaintiff read the earlier policy or the quotation, it would have been obvious that "full replacement value" was clearly not included in the policy, constituting not only comparative negligence but also the proximate cause of plaintiff's loss. Reciting the general rule that an agent "owes no duty to advise a potential insured about any coverage" and the exceptions to the rule,<sup>29</sup> the court, relying on *Harts v. Farmers Insurance Exchange*<sup>30</sup> agreed that the special relationship creates a duty to give advice in certain circumstances. The jury in the underlying action found that a special relationship existed. The appellate court rejected Zaremba's argument that the finding of a special relationship eliminated the claim of comparative fault concomitant with the duty on the part of the insured to read its insurance documents.<sup>31</sup>

... we view as simply illogical the suggestion that the agent's decision to undertake additional responsibilities on behalf of an insured immunizes the insured from the consequences of its own negligence. The negligence of one party does not eliminate the legal requirement that an opposing party use ordinary care.<sup>32</sup>

The court reversed the judgment in favor of the plaintiff on the negligence and other claims and remanded the matter for a new trial.

The Court of Appeals of Washington addressed the question of adequacy of limits of a homeowners policy in the matter of *McClammy v. Cole*. Plaintiffs, Richard and Mary Lou McClammy, appealed from a dismissal of their claims based upon the special relationship, against Michael Cole and State Farm Fire and Casualty Company. The Court affirmed the lower court's decision, finding that, absent a special relationship, an insurance agent has no obligation to recommend limits higher than those chosen by the policyholder.<sup>33</sup> When plaintiffs purchased their home in 1995 for \$248,000, Cole provided three quotes with limits from \$190,000 to \$225,000. The McClammys chose a \$200,000 replacement cost policy. Over several years, improvements were made to the property, although this was not made known to Cole until a meeting in May 2004 with Mr. McClammy. The primary purpose of the meeting was to discuss the increase in premiums and how to reduce them, although the improvements were discussed in general. At that time, the home was insured for \$275,200. After the meeting, at McClammy's request, Cole sent an e-mail providing information on previous coverage rates and premiums and further indicated that based on the information provided by Mr. McClammy, the limits could be reduced to \$240,200 "and still stay within an estimated 100% to value."<sup>34</sup> The home was completely destroyed by a fire on April 5, 2005. Based on contractors' estimates, the cost to rebuild the home exceeded the policy limits by \$213,000. In seeking the excess over policy limits, the McClammys relied solely on the special relationship. The court stated:

A special relationship exists if (1) the agent holds himself out as an insurance specialist and receives additional compensation for consulting and advice, or (2) there is a long-standing relationship, some type of interaction on the question of coverage, and the insured relied on the agent's expertise to the insured's detriment.<sup>35</sup>

Although the court agreed that there was a long-standing relationship and that there was some sort of interaction on the question of coverage, the facts did not support a finding that the policyholders ever consulted with Cole about the adequacy of coverage and further that Cole did not provide any advice in that regard. Without this type of interaction, the special relationship could not be supported.<sup>36</sup>

## Defining the Special Relationship—The Policyholder and the Producer

Almost universally, an insurance agent's legal duty is to follow his or her client's instructions and to obtain the best insurance available at the most commercially reasonable price and terms using reasonable skill and ordinary diligence. There is no additional "legal" duty to provide unsolicited advice: ". . . it is well settled that agents have no continuing duty to advise, guide, or direct a client to obtain additional coverage."<sup>37</sup> Under certain circumstances, however, a special relationship can be created between the insured and the insurance producer, thereby altering the producer's legal duty by adding a legal duty to provide advice to the insured.<sup>38</sup>

Before discussing the criteria necessary to establish the special relationship, it is important to understand what the special relationship is and what it is not. The special relationship is not a basis for post-loss underwriting. Assertions of the special relationship usually include allegations (i) that the producer should have advised the insured to purchase certain specific coverage or adequate limits; (ii) that if the insured had been so advised, the coverage and/or limits would have been purchased; and (iii) that if the coverage had been purchased and available,<sup>39</sup> the result would have been that an underinsured or disputed claim would have been paid by the insurer. However, in situations in which the facts support the existence of the special relationship, any

claim against a producer is fortified because of the additional legal duty imposed on the producer. The special relationship, once established, can eliminate the need for proof of a violation of the standard of care by the producer.<sup>40</sup> Consequently, assertions of a special relationship are often added to a complaint against a producer even without any factual underpinning as a tactic to gain a favorable settlement.

When considering whether to bring an action against an insurance producer based on the special relationship, the practitioner should carefully evaluate the use of the “expert” description as a substitute for actual facts supporting the special relationship. That the producer is an “expert” should have a logical nexus to the insurance being procured; otherwise, the court may easily find only the typical policyholder-producer relationship. For example, an insurance producer who procures a package policy for a restaurant, a dry cleaner, an office building, or other common types of businesses ordinarily does not need special expertise to procure such insurance and is ordinarily not an “expert,” despite allegations to the contrary. The “expert” appellation is more appropriate in areas of specialized coverages not dealt with on a regular basis by most insurance producers, such as motor truck cargo, ocean marine, or aviation exposures.<sup>41</sup> As the reviewed cases suggest, in order to establish the special relationship, more than the typical policyholder-insurance agent association must be demonstrated.

## The Special Relationship, Coverages, and Policy Limits

The decisions uniformly distinguish between advice as to coverages and recommendation as to limits. For example, the Maryland Court of Special Appeals dealt with the subject of the special relationship in *Sadler vs. The Loomis Company*, 139 Md.App. 374, 776 A.2d 25, (2001). Evelyn Sadler had been a client of the Murray Agency<sup>42</sup> through her family business as well as personally for over fifty years, purchasing both homeowners and automobile insurance. Until The Loomis Company purchased the Murray Agency in 1987, there were regular meetings with a Murray producer who delivered the policies. This practice stopped with Loomis, contact being limited to times when she had a question concerning her insurance, and then only by phone or letter. On May 13, 1996, Sadler had an at-fault accident with a motorcyclist, Timothy Prophet, resulting in amputation of one of the motorcyclist’s legs. At the time of the occurrence, Sadler had automobile liability limits of \$100,000.<sup>43</sup> In 1999, Sadler settled Prophet’s claim for \$1 million, which included the \$100,000 from her automobile insurer. Sadler then sued Loomis, claiming it was negligent because it was aware of her financial position and “failed to provide her with periodic quotes as to the cost of additional protection, or sufficient information to enable her to make an informed decision as to the appropriate level of liability coverage.”<sup>44</sup> The Court held “that, in the absence of a special relationship, an insurance agent or broker has no affirmative, legally cognizable tort duty to provide unsolicited advice to an insured regarding the adequacy of liability coverage.”<sup>45</sup>

The court further opined that:

A “special relationship” within the insurance industry is an important concept. A special relationship in the context of insurance requires more than the ordinary insurer-insured relationship. It may be shown when an insurance agent or broker holds himself or herself out as a highly skilled insurance expert, and the insured relies to his detriment on that expertise. A special relationship may also be demonstrated by a long-term relationship of confidence, in which the agent or broker assumes the duty to render advice, or has been asked by the insured to provide advice, and the adviser is compensated accordingly, above and beyond the premiums customarily earned. (Citations omitted)<sup>46</sup>

Citing with approval from *Parker v. State Farm Mut. Auto. Ins. Co.*, 630 N.E.2d 567, 569-570 (Ind.Ct.App. 1994), the Court continued:

[It] is the nature of the relationship, and not merely the number of years associated therewith, that triggers the duty to advise. Some of the factors relevant to developing entrustment between the insured and the insurer include: exercising broad discretion to service the insured's needs; counseling the insured concerning specialized insurance coverage; holding oneself out as a highly-skilled insurance expert, coupled with the insured's reliance upon the expertise; and receiving compensation, above the customary premium paid, for expert advice provided. (Internal case citations omitted)<sup>47</sup>

What can be gleaned from the case law is that the producer has no legal duty to give advice to the insured unless special circumstances or a special relationship exists. In discussing the duty to advise of possible additional coverage needs, New York's highest court, in the case of *Murphy v. Kuhn*, pithily stated: "[Insurance agents] are not personal financial counselors and risk managers, approaching guarantor status."<sup>48</sup>

The general rule is well stated in a 1997 California appellate decision, *Fitzpatrick v. Hayes*:<sup>49</sup>

[A]s a general proposition, an insurance agent does not have a duty to volunteer to an insured that the latter should procure additional or different insurance coverage. . . . The rule changes, however, when—but only when—one of the following three things happens: (a) the agent misrepresents the nature, extent or scope of the coverage being offered or provided, . . . (b) there is a request or inquiry by the insured for a particular type or extent of coverage, . . . or (c) the producer assumes an additional duty by either express agreement or by "holding himself out" as having expertise in a given field of insurance being sought by the insured.

The producer is protected by the body of laws discussed above, which set forth the seminal duties of a producer and acquit the producer of responsibility for rendering unsolicited advice to a client. The responsibility for decisions concerning the selection of insurance coverages offered by the producer and the selection of limits rests solely with the insured. In most jurisdictions, it is the responsibility of the customer to read the policy to determine, among other things, that the coverages and limits are those that have been requested.

The analysis used by the court in *Southwest Auto Painting and Body Repair*, supra, provides the practitioner with a means to sidestep the difficulty in establishing the special relationship. By framing the producer's failure to provide advice as a standard of care issue, there would be no need to rely on the special relationship: the finder of fact could find that a failure to provide advice was a clear-cut violation of the standard of care not dependent upon the special relationship.

## Risk Management and the Special Relationship

Although not explicitly addressed in the above reviewed cases, and largely overlooked, when an insurance producer purports to act as a risk manager, either demonstrably or by default, a special relationship can be created.<sup>50</sup> However, there is a clear delineation between a risk analysis performed by an insurance producer and a risk management assessment performed by a risk manager. The approach used by both the producer and risk manager is deceptively similar to what is used by the consumer, but the methodology used, analysis performed, and results offered by the risk manager are considerably more extensive, and the outcome can be distinctly different. In order to understand the scope of the risk manager issue, a definition of risk management is instructive:

Risk Management is the systematic, problem-solving process used to identify and treat the pure loss exposures of an organization or individual; it has six steps: identify loss exposures, analyze or measure loss exposures, consider the risk treatment alternatives, select the best combination of risk treatment alternatives, implement the decision and monitor the program.<sup>51</sup>

Under most circumstances, an insurance producer is not a genuine risk manager unless that individual has received training and/or has been certified as a risk manager and the agent has unmistakably agreed to act in that capacity. A risk manager is an individual who, by education and/or training, has: (a) a background in insurance; (b) an ability to identify all patent, as well as latent, exposures; (c) knowledge of the available various risk transfer methods and when to recommend each; and (d) an operating knowledge of all insurance coverages available to the sector in which the risk manager is employed. There are, however, marked differences between the insurance producer's and the risk manager's guidance for an insured. Insurance is the most commonly accepted form of risk transfer and is the exclusive method employed by the insurance producer on behalf of a client. A risk manager, on the other hand, has a number of risk transfer or risk treatment methods not usually offered by the insurance producer: (1) loss control, (2) avoidance, (3) retention, (4) noninsurance transfer (i.e., indemnity, hold-harmless agreements), and (5) insurance. In other words, a risk manager tries to avoid using insurance, the goal being to reduce the cost of risk, not to sell insurance. Compare these tasks with the goal of an insurance producer whose sole function is to protect the client through the exclusive use of insurance.

Incongruous as it may seem, even though the insured may believe that the producer is functioning as a risk manager, unless agreed to in advance, the producer assumes no risk management duties in the legal sense. Whether the producer is considered a risk manager depends, at least in part, upon how the consumer/insured perceives the role of the producer and whether this perception is expressed to the producer by the insured and/or by the producer to the insured. Full disclosure by the insured or prospective insured of the parameters of his or her reliance is a prerequisite in those instances in which the insured claims that the producer agreed to act as a risk manager.

According to Madelyn Flanagan of the Independent Insurance Agents of America, "Risk analysis is an everyday part of what [independent agents] do. It has always been a part of what they do on behalf of a commercial client. . . ." <sup>52</sup>

Historically, the client perceives that the producer is acting as a risk manager. Most clients equate the assistance provided by an insurance producer as "risk management" services and do not know the difference. In other words, the producer acts as an *ad hoc* risk manager, and the insured forms the opinion that risk management services are being provided. Neither acknowledges that risk management is or is not occurring. External pressures, such as insurance market conditions, competition, mergers of companies with subsequent reduction of markets, and mergers of agencies have forced the producer to imitate a risk manager in many commercial and, to a lesser extent, personal lines account situations. In these instances, the application of the factual circumstances to the legal duty will be determinative of the producer's liability.

## The Special Relationship in Federal Courts

It will be problematic for federal plaintiffs to effectively plead the special relationship as well as to avoid a successful 12(b)(6) motion to dismiss. Unlike most state plaintiffs, federal plaintiffs will have a difficult time overcoming a motion to dismiss the special relationship allegations because of the holdings in *Bell Atlantic Corp. v. Twombly*, 129 S.Ct. 1937, 173 L.Ed2d 868 (2007) and *Ashcroft v. Iqbal*, 550 U.S. 554, 127 S.Ct. 1955, 167 L.Ed2d 870 (2009).<sup>53</sup> Practitioners will be required to provide facts that support the allegations of a special relationship: allegations such as that the producer held himself or herself out as an "expert," that the insured depended on the producer and his/her expertise, that the producer was previously an insurance underwriter, that the producer recommended that the insured purchase certain coverages but failed to suggest others, and/or that there is a long-standing relationship between the agent and the insured are



simply not sufficient based on the case law in most jurisdictions to sustain a claim based on the special relationship.

**Real-world examples:** Below are characteristic allegations from a state and a federal lawsuit that purport to represent a colorable claim that a special relationship existed between the insurance producer and the client.

In the first example, filed in state court, the client/policyholder is the owner of a restaurant, the building housing the restaurant, and substantial business personal property:

Through Defendants' actions and interactions with the Plaintiffs, Defendants cultivated and created a special relationship with the Plaintiffs, such that Plaintiffs reasonably relied upon the advice and recommendations of the Defendants to select and produce an appropriate type and amount of insurance coverage for their business and property. Defendants undertook to counsel Plaintiffs on their specialized insurance coverage needs, and Defendants were given broad discretion to procure insurance that would protect [Plaintiffs].

The policyholder started in the restaurant business in 2002, when he assumed a lease and purchased an ongoing restaurant business. In 2005, the policyholder purchased a building and moved the restaurant to this new location. From 2002 until the end of 2007, the policyholder used the services of a producer referred by the individual from whom the insured purchased the business. At the end of 2007, the policyholder changed producers to the defendant. In early 2009, the building housing the restaurant was substantially damaged by fire, and the business personal property was destroyed. According to the insured and his public adjuster, the building and business personal property were significantly underinsured.<sup>54</sup>

The insured restaurant owner testified during deposition that he had never read any insurance policy provided to him by either the previous producer or the defendant. In arriving at the values for the building and business personal property, the defendant producer, with the approval of the insured, used the limits of the expiring policy as baseline limits of the policy he procured for the plaintiff. The producer asserted that he reviewed the policy, including limits, with the insured both before the policy was procured as well as when the policy was delivered and at the subsequent renewal. When pressed during his deposition for particulars that might support a special relationship, the policyholder was unable to identify a single fact to support a special relationship. Allegations were also made in the complaint that payments were provided to the producer in addition to commissions, allegations that turned out to be fabricated and that were ultimately withdrawn. Furthermore, the policyholder stated that he did not give the producer the power to make any decisions with respect to insurance.

By the plaintiff simply suggesting in his complaint that a "special relationship was cultivated," a dismissal on the pleadings may have been avoided, but these threadbare allegations cannot ultimately sustain the evidentiary burden imposed on the plaintiff to prove a genuine special relationship. The case settled prior to trial.

A second example involves a federal district court multimillion-dollar lawsuit filed against an insurance producer by a religious order<sup>55</sup> for underinsured losses suffered by its religious school in New Orleans caused by Hurricane Katrina. Both the order and the school were plaintiffs:

- Defendant represents that it specializes in insurance coverage for religious, charitable and academic institutions. Defendant represents that it understands "the unique challenges of managing the risks that the academic world addresses every day" and purports to "deliver innovative solutions to meet those demands." Defendant also represents that it specializes "in providing long-term, stable, and affordable solutions of risk management and insurance programs" for religious and charitable organizations.

- For over fifty years, Defendant has been the insurance broker, consultant and advisor for the Plaintiffs. At all times relevant hereto, Defendant has held itself out and represented to the Plaintiffs and The School as having special expertise in the insurance requirements of religious and academic institutions, particularly Catholic institutions.
- At all times relevant hereto, Defendant has understood, acknowledged, and represented that it had a special relationship with [both] The School and the Plaintiff whereby Defendant had a professional and contractual obligation to review coverage for Plaintiff and The School, evaluate that coverage and recommend any necessary or useful changes in policy limits, scope of coverage, or type of coverage, all in order to make sure that The School and the Plaintiff had the necessary and requisite insurance coverage to protect their interests.
- Defendant intended and knew that The School and the Plaintiffs relied on Defendant's expertise and trusted that Defendant would regularly review their insurance coverage and make all necessary and expected recommendations and would, due to their special relationship, do nothing to harm The School and the Plaintiff.
- [NEGLIGENCE AGAINST AGENT] Professional insurance brokers, advisors, and consultants such as Defendant are considered fiduciaries and are, therefore, held to a standard of care higher than the ordinary standard of care. Defendant, as an insurance broker and/or consultant with a long-term, special relationship with The School and the Plaintiffs, was obligated to exercise fiduciary duties of good faith, reasonable skill and diligence in dealing with The School and the Plaintiff.

The producer in this lawsuit had not procured business interruption coverage for the religious school, and the purported business income/tuition loss was alleged to have been in excess of \$2 million. A representative of the producer testified at his deposition that business interruption coverage and limits had been discussed several times and that the Order was aware of such coverage and had rejected it on several occasions. The Order disputed these statements. An interesting facet of the claimed damages for the business income loss was that many of the students who had been relocated to other areas of Louisiana as well as other states did not return to New Orleans, thus decreasing the available student base with a subsequent continued loss of tuition income. The school was able to continue to function after a few weeks post-Katrina by first relocating to a facility in an undamaged area outside of New Orleans and by then reopening once repairs had been accomplished. A separate issue concerned the scope of the business interruption claim and whether this was appropriate to factor in to the overall claim. To avoid these issues, considerable emphasis was placed on the special relationship by the plaintiff in order to circumvent the myriad of factual inadequacies in its case. In its answers to interrogatories, the plaintiff Order, in support of its special relationship allegations, referred to the producer's website, which touted the producer's extensive knowledge and expertise in insuring religious institutions and religious schools, and the use of the term "expert." The latter might have been of some aid to the plaintiff had any individual within the Order been aware of or accessed the website.

Plaintiff alleged that the agent should have advised the plaintiff of the available time element coverage and recommended that it be purchased based on the existence of the special relationship, consequently rendering the factual disputes moot. Plaintiff held its ground on the special relationship issue through the paper discovery phase, but it unraveled during depositions of the priests who were responsible for procuring insurance through the producer.

Using the guidance set out in *Sadler, supra*, defense counsel was able to highlight the abject failure of a factual predicate necessary to establish the special relationship. In order to support a finding that a special relationship existed, the designated representative of the Order during his deposition testified to four examples: the producer had procured flood insurance post-Katrina, had periodically reviewed with the Order the values it had set for its various properties, had addressed the Order's concern over sexual abuse coverage and limits, and had raised and discussed terrorism coverage. The deponent could not point to a single instance when the defendant was made aware of the potential existence of the special relationship. Prior to defendant's counsel filing several dispositive motions, including one based on *Iqbal, supra*, the parties settled the matter.

## Conclusion

Care should be used by the practitioner before building an entire case against an insurance agent on the special relationship or when deciding to add allegations that a special relationship supports claims of breach of contract, negligence, or the other available tort and contract remedies. Using the special relationship as the only basis for a lawsuit against a producer is a daunting challenge but in some situations might be a worthwhile exercise. State courts, as opposed to federal courts, are generally more inclined to allow a case to proceed beyond the motions stage even when there is slight verifiable substance to the claim of a special relationship. However, once past the motions stage, the lawsuit achieves a basis on which settlement must eventually be considered by defense counsel. Nonetheless, a settlement in an E&O case is more difficult to achieve than in a conventional negligence case: before any E&O case can be settled, the terms and conditions of the producer's claims made policy—which often include a loss or combined loss/litigation deductible that must be paid by the producer—the producer's control over any potential settlement, and the applicability of a hammer clause and the company's willingness to use it must be addressed. Relying on the special relationship where none exists offers only an illusory weapon to a plaintiff's attorney that, when wielded, creates an additional workload for both parties and that, without a strong factual base, can lead to an embarrassing situation, either during deposition, during motions hearings, or at trial.

## Endnotes

- (1) Since a majority of states have passed or employed the National Association of Insurance Commissioners (NAIC) Producers Licensing Model Act, which defines insurance agents and brokers collectively as an insurance producer, for the purposes of this article, the terms "agent" and "broker" are used interchangeably along with the term "producer."
- (2) See *Bruner v. League Insurance Company*, 164 Mich. App. 28, 416 N.W.2d 318 (1987), *Rawlings v. Fruhwirth*, 455 N.W.2d 574 (N.D., 1990), *Southwest Auto Painting and Body Repair, Inc. v. Binsfeld*, 183 Ariz. 444, 904 P.2d 1268, (Ariz. App. Div.1, 1995), *Trupiano v. Cincinnati Insurance Company*, 654 N.E.2d 886 (Ind. App. 1995), *Murphy v. Kuhn*, 660 N.Y.S. 2d 371, 90 N.Y.2d 266, 682 N.E.2d 972 (1997), *Harts v. Farmers Ins. Exchange*, 461 Mich.1, 597 N.W.2d 47(1999), *Peter v. Schumacher Enterprises, Inc.*, 2001 Alaska 160 (2001), *Sadler vs. The Loomis Company*, 139 Md.App. 374, 776 A.2d 25, 1 (2001), *Sintros v. Hamon*, 810 A.2d 553 (N.H., 2002), *Zaremba Equip. v. Harco National Insurance Company*, 280 Mich. App.16, 761 N.W.2d 151, (2008), *Axis Construction Corp. v. O'Brien Agency, Inc.*, 2009 NY Slip Op 32491 (N.Y. Sup. Ct.10/21/2009), (N.Y. Sup. Ct., 2009), *McClammy v. Cole*, 243 P.3d 392, 158 Wash. App.769 (Wash.App 2010). These cases are representative of the law in various jurisdictions but are not intended as an exhaustive collection.
- (3) *Bruner* at p. 319.
- (4) *Id.* at 321.
- (5) *Rawlings* at 575. The allegations included failure to procure requested insurance, failure to protect against gaps in coverage, and negligent misrepresentation as to the availability of insurance.

- (6) Id.
- (7) Id. at 579.
- (8) Id. 578.
- (9) *Southwest Auto Painting* at 1272.
- (10) Id. at 1269.
- (11) Id. at 1270.
- (12) Id.
- (13) Id. at 1270. The court quoted language from *Markowitz v. Arizona Parks Board*, 146 Ariz. 352, 706 P.2d 364 (1985): “the existence of a duty is not to be confused with details of the standard of conduct. Duty is found in the relationship between individuals that ‘imposes upon one a legal obligation for the benefit of the other . . . . Details of conduct . . . have to do with whether the defendant breached the applicable standard of care, not whether a duty and attendant standard of care exist” (citations omitted).
- (14) *Trupiano* at 887.
- (15) During the 1985 to 1989 time period, Trupiano met with another agent from Alkema’s agency, SZW.
- (16) *Trupiano* at 888.
- (17) Id.
- (18) Id.
- (19) The *Murphy* case is also referred to in the body of this article.
- (20) *Murphy* at 373.
- (21) Id. at 374.
- (22) *Peter*, headnote [52].
- (23) Id. headnote [56].
- (24) *Zaremba* at 155.
- (25) Id. at 156
- (26) Id. at 157.
- (27) Id.
- (28) Defendant also raised challenges to the fraud and innocent misrepresentation verdicts, promissory estoppel, plaintiff’s failure to present expert testimony, and plaintiff’s claims for breach of contract, recovery of insurance premiums, and penalty interest. Only the negligence issue is addressed in this article.
- (29) *Zaremba*. at 159. The change in the agent-insured relationship occurs when “(1) the agent misrepresents the nature or extent of the coverage offered or provided, (2) an ambiguous request is made that requires 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 by express agreement with or promise to the insured.” (citations omitted)
- (30) 461 Mich.1, 597 N.W.2d 47(1999),
- (31) Id.
- (32) Id. at 160.
- (33) *McClammy* at 158 Wash.App. 774.
- (34) Id.at 772.
- (35) Id. at 774, quoting *Lipscomb v. Farmer’s Ins. Co. of Wash.*, 142 Wash.App.20, 28, 174 P.3d 1182 (2007).

- (36) The *McClammy* opinion provides a pithy review of Washington State case law involving the special relationship; the opinion itself is slightly more than five pages.
- (37) *Murphy v. Kuhn*, 660 N.Y.S.2d 371, 375.
- (38) Even when the special relationship is found to exist, the selection of policy limits universally remains the function of the insured, not the insurance agent or broker. There may be isolated situations in which the agent or broker has unequivocally agreed to take on this responsibility, but these instances are the exception. When there is no clear agreement to the contrary, selection of limits is the policyholder's responsibility.
- (39) Most practitioners assume that the alleged missing coverages and/or higher limits are readily available, which may not be accurate and should be confirmed.
- (40) In many jurisdictions, proof of a producer's failure to meet his or her legal duty is sufficient to allow the finder of fact to consider the producer's culpability in an E&O case. There would be no need for an expert witness to opine with respect to a producer's breach of the standard of care. See fn. 13.
- (41) See *Johnson & Higgins v. Hale*, 121 Md.App. 426, 710 A.2d 318 (1998), *International Brotherhood of Teamsters v. Willis Corroon Corporation of Maryland*, 369 Md. 724, 802 A.2d 1050 (2002)
- (42) The original agency name was E. Churchill Murray, later Murray, Martin & Olsen.
- (43) Sadler's home was valued at over \$600,000 and was insured for \$231,000.
- (44) 139 Md.App. at 374.
- (45) *Id.* at 374,410.
- (46) *Id.* at 393.
- (47) *Id.* at 394.
- (48) 660 N.Y.S.2d at 375.
- (49) 57 Cal.App.4th 916, 67 Cal.Rptr.2d 445, 452 (1997).
- (50) Agreeing to act as a risk manager would bring the producer within the ambit of the general rule set out in *Fitzpatrick v. Hayes* cited on this page, particularly paragraph (c).
- (51) Burnham's Insurance Dictionary, Burnham (2009)
- (52) Madelyn Flanagan, Assistant vice president for research, IIAA, quoted in Roquet, Deregulation Could Put Agents on the Spot, *National Underwriter*, September 4, 2000.
- (53) For an in depth discussion of the effects of these two cases See: *Convoluted Court*, Leslie Gordon, *ABA Journal*, January 2011, p. 16
- (54) The insurer estimated the loss to be approximately five percent higher than the policy limits for the building. The policyholders' public adjuster calculated that the building was underinsured by more than one half.
- (55) The religious order was located in Maryland and made all decisions with respect to procuring insurance for a School located in New Orleans. The school was a separate corporate entity, but was governed by the order's six member General Council. The Council also functioned as the board of trustees of the School which had very little input into the selection of insurance coverage and limits.