The hidden defendant

Insurance brokers are the middlemen we often overlook when a claim is denied

By Demián Oksenendler

Many of us in the insurance bar live with a set of gloomy expectations around the seasons. Years of witnessing changing climate, corporate mismanagement, misguided (though perhaps well-intentioned) government policy, and plain bad luck, keep us attuned to a grim cycle: Every year, like clockwork, the seasons change, and we follow quickening pattern of hurricanes in the South and East, tornadoes and floods in the Midwest, snowstorms in the North, and, of course, wildfires and mudslides in the West. To make matters worse, it seems every year these disasters grow increasingly severe.

The disasters we see dominating the news cycle (and, sadly, increasingly experience on a first-hand basis) also spin off countless legal disputes. Many of those disputes center around insurance policies. Individuals and businesses buy insurance in hopes of protecting themselves, their assets, and the people they care about. It is only when disaster strikes that they frequently discover that the insurance they wanted, and believed they had, is insufficient or not there at all.

Sometimes, the problem is that the policy itself does not cover the loss. Other times, the problem is the way an insurance carrier or adjuster has decided to handle a particular claim. And, sometimes, the problem is with the transaction that produced the insurance policy itself.[1] I sometimes call insurance agents and brokers (the people who sell insurance policies) "hidden defendants," because they can be so easy to overlook. The insurers are the ones that deny or restrict coverage, so the clients are focused on them. That is where most of the correspondence and documents are. And, sometimes, losses occur long after the insurance policies at issue were sold, so the transaction itself is a distant memory. Yet, sometimes that transaction is the root cause of the client's problem. Those hidden defendants are the focus of this article.

Nature of the relationship

California law recognizes multiple categories of sellers of insurance (also called "producers"). An insurance "agent" is distinct from an insurance "broker" in

that an agent works for the insurer (think State Farm agent), while a broker works for the insured.[2] The hallmark of an agency relationship is an appointment by an insurer to transact business in its behalf.[3] It is "not uncommon", however, for those who sell insurance to be dual agents.[4] Generally, the determination of which category a producer falls into is an issue of fact in each case.[5] Indeed, dual agency is so common in the area of property and casualty insurance (which covers first party claims, such as fires) that our Legislature created the title of "property broker-agent" for professionals in that field.[6]

General duties

Irrespective of which designation an insurance producer ultimately holds, there are certain rules that apply to producer-client relationships. In California, insurance producers are a species of professional. Consequently, they have a duty "to use reasonable care, diligence, and judgment in procuring the insurance requested by an insured."[7] A key part of that sentence that is often overlooked is the word "requested." Insurance producers are not advisors and are not fiduciaries.[8] An insurance producer does not have a duty (absent special circumstances, discussed below) to advise about or recommend any type of amount of coverage.[9] Indeed, public policy militates against it.[10]

So, how can an insurance producer be liable when a claim goes wrong? An insurance producer breaches his/her/its duty by misrepresenting the nature, extent, or scope of coverage, or failing to procure specific coverage requested.[11] Also, since insurance producers (like many other professionals) do their work out of the client's view, there is a disparity of knowledge about the process. Clients tell insurance producers what their needs are, and then trust those producers to go out into the insurance marketplace to find and deliver coverage to match. Clients are not involved in the process and do not know the details of what goes on. Consequently, producers that fail to deliver coverage that is promised or agreed-upon, without warning their clients, are also liable for resulting harm.[12]

Also, an insurance producer must tell the truth about the insurance sought by or obtained for a client. "The agent's duty is 'reasonably to inform an insured of the insured's rights and obligations under the insurance policy.'"[13] When a client asks a broker questions, the producer has a duty to respond truthfully, completely, and with reasonable care.[14] By that same token, clients have the right to rely on the representations that insurance producers make. Absent some notice or warning" it is not the client's responsibility to read the policy language to verify that the coverage delivered matches what the client requested or what the producer represented.[15]

Special relationship

The duties of an insurance producer are elevated when there is a "special relationship" between them and the client. Those elevated duties can include the obligation to advise their clients about the scope and adequacy of coverage, including gaps in coverage and missing coverages the client needs. This analysis is rarely straightforward, and can turn on a number of factors (none of which need be individually dispositive), including:[16]

- Length of course of dealing generally.
- Whether the course of dealing indicated the client relied on the broker's advice.
- Communications between broker and client.
- Whether the broker received greater compensation than normal, or above the amount of premium.
- Whether the broker holds him/her/itself out as an expert.
- Whether the client specifically requests advice.
- Representations by the broker regarding the coverage obtained/promised upon which the client relies.

All the above factors and angles deserve a careful examination when considering whether a potential client has a claim against an insurance producer. Balancing them to reach a conclusion is an exercise in good judgment, good experts, [17] and plain-old common sense.

For example, I recently was able to resolve a case based in large part on the special relationship doctrine. In that case, the client (a wealthy businessperson with a complex mix of personal and business insurance policies) had relied on the same insurance broker for decades and had never "shopped" their business to others. Moreover, the client had been paying full-price commissions for all that time. Those two factors helped demonstrate that the insurance broker involved was more than just a salesperson or order-taker. The degree of reliance there, along with the well-above-market commissions the broker was collecting, helped establish that the broker was really an advisor who should have recommended a certain coverage to the client that was missing at the time the client needed it most. That change in status also helped overcome ambiguities in the paper trail and other challenges in proving whether the client had requested or been promised the coverage at issue.

The technology advantage of e-mail and texting

Modern technology has given us one of the best sources of evidence for establishing insurance producer liability: e-mail and text messages. In days gone by, insurance producers and their clients interacted mostly in person or over the phone. The only written materials they would generate would often consist of just an application form (usually filled out by the producer). There would be no record of what the client requested, or what the producer promised.

E-mail and text messages have completely changed the game. Now, we often have a clear paper trail of what the client asked for, what the producer

promised, and all of the explanations in between. Furthermore, unlike letters, the sender will almost always have a copy of the entire thread of communications in one place. I have had the good fortune to handle multiple cases that have resulted in successful outcomes based on the e-mails and text messages exchanged with insurance producers. Most of them would have gone nowhere otherwise. These days, when I meet a client considering litigation against an insurance producer, e-mails are among the first things I request.

Licensing and negligence *per se*

In addition to the relationship between the parties, licensing issues can be decisive. Individuals and businesses that transact insurance in California must be licensed (indeed, it is actually a misdemeanor to do so without one).[18] There are a number of different license categories in California, the most common being property and casualty, life, and Accident & Health. A special license and other disclosures are required for those who wish to place insurance policies that have not been approved by the Department of Insurance.[19] These are called "surplus lines."

Our Legislature has defined the term "transact" to include "transaction of matters subsequent to the execution of the contract and arising out of it."[20] Procuring insurance for a client is "transacting" insurance.[21] Collecting premiums and executing endorsements are also forms of transacting insurance.[22] Furthermore, since at least the 1960's, the California Attorney General has taken the position that even issuing certificates of insurance is also a form of transacting insurance.[23] Additionally, insurance producers owe a duty to third parties, and are liable to them on a negligence *per se* theory when they place insurance in violation of the Insurance Code.[24]

When considering a potential claim against an insurance producer, licensing is always where I start. An unlicensed sale is *per se* negligent, and that can put the brakes on defense arguments about causation. When the producer goes through with a transaction they should have declined, it leaves very little room for them to try justify anything they did afterward. In addition, if an unlicensed producer is an insurer's agent (see above), that opens up the possibility of holding the insurer vicariously liable for the producer's conduct.[25] The potential for an insurer to be liable for an unlicensed sale of its policies (and the accompanying danger of regulatory or class/mass action consequences that could follow), can be a powerful advantage for a client. The "hidden defendant" can make it possible to hit a much bigger target.

Damages

Damages in cases involving insurance producers can be tricky. Like most professional negligence cases, clients are entitled to be put in the position they would have occupied but for the producer's conduct. However, there are limitations. Unlike insurers, that can be subjected to liability beyond policy limits[26], insurance producers are generally only responsible for the coverage that the client would have had if the producer had not breached its duty.[27]

Consequently, if the insurance that the client contends should have been in place would have been prohibitively expensive; or if the insurance would not be available at all, then damages could be seriously limited. It is critical when evaluating a potential case against an insurance producer to engage an expert who can opine on the availability and price of the insurance at issue.

One type of damages that can be recovered from insurance producers that are not available in most situations is attorney fees. These are available under a variation on "tort of another doctrine." In California, attorney fees incurred through instituting or defending an action as a direct result of the tort of another party are recoverable damages.[28] Attorney fees are recoverable as damages from insurance producers if:

1. An insurance producer sells a policy that is ambiguous;
2. The client has to litigate with their insurer in order to obtain benefits;
3. The insured is successful in the litigation against the insurer; *and*
4. The producer could have obtained coverage that unambiguously covered the loss.

In such cases, the client can recover from the producer *only* those attorney fees incurred in the litigation *against the insurer.*[29]

Conclusion

Insurance producer litigation is both complicated and rewarding. It requires an understanding of the nature of the relationship of the parties, the right places to look for evidence, careful analysis of the damages, good experts, and good sense. When handled properly, the pursuing a claim the "hidden defendant" can be the key to making your clients whole again after a loss.

Demián Oksenendler is a partner at San Francisco's Mannion Lowe and Oksenendler *where he specializes in insurance coverage and bad faith. He is a 2004 graduate of Hastings College of the Law and has been named a Rising Star by Super Lawyers.*

Oksenendler

Endnotes: [see next page]

[1] These issues are, of course, not unique to hazard insurance. The same issue arises in the context of liability insurance as well. Every day, insurers reject or restrict coverage on innumerable third party claims.

[2] Cal. Ins. Code §§ 31, 33. A "dual agent" works for both. *Kurtz, Richards, Wilson & Co. v. Ins. Communicators Marketing Corp.* (1993) 12 Cal.App.4th 1249, 1257; *Loehr v. Great Republic Ins. Co.* (1990) 226 Cal.App.3d 727, 734; *Lippert v. Bailey* (1966) 241 Cal.App.2d 376, 383.

[3] Cal. Ins. Code § 1731; *Marsh & McLennan of Cal., Inc. v. City of Los Angeles* (1976) 62 Cal.App.3d 108, 113, 117-118.

[4] *Kurtz*, 12 Cal.App.4th at 1257.

[5] *Arocho v. Cal. Fair Plan Ins. Co.* (2005) 134 Cal.App.4th 461, 466

[6] Cal. Ins. Code §§ 33.5, 1625.

[7] *Mark Tanner. Constr., Inc. v. HUB Int'l Ins. Svcs., Inc.* (2014) 224 Cal.App.4th 574, 584.

[8] Except with respect to ensuring premiums it holds are delivered to the insurer or premium refunds are returned to the client. Cal. Ins. Code §1733; *Van de Kamp v. Bank of America* (1988) 204 Cal.App.3d 819, 863.

[9] *Fitzpatrick v. Hayes* (1997) 57 Cal.App.th 916; *Ahern v. Dillenback* (1991) 1 Cal.App.4th 36.

[10] *Schultz Steel Co. v Hartford Acc. & Indem. Co.* (1986) 187 Cal.App.3d 513.

[11] *Mark Tanner Const.* 224 Cal.App.4th at 584; *Desai v. Farmers Ins. Exch.* (1996) 47 Cal.App.4th 1110, 1119-1120; *Nowlon v. Koram Ins. Ctr., Inc.* (1991) 1 Cal.App.4th 1437, 1447; *Greenfield v. Insurance, Inc.* (1971) 19 Cal.App.3d 803, 811.

[12] *Butcher v. Truck Insurance Exchange* (2000) 77 Cal.App.4th 1442, 1461.

[13] *Butcher*, 77 Cal.App.4th at 1462 (internal citation omitted).

[14] *Westrick v. State Farm Ins.* (1982) 137 Cal.App.3d 685; *Free v. Republic Ins. Co.* (1992) 8 Cal.App.4th 1726, 1729; *Clement v. Smith* (1993) 16 Cal.App.4th 39; *Paper Savers, Inc. v. Nacsa* (1996) 51 Cal.App.4th 1090; *Fitzpatrick*, 57 Cal.App.4th at 922.

[15] *See, e.g., Williams v. Hilb, Rogal & Hobbs Ins. Services of Cal., Inc.* (2009) 177 Cal.App.4th 624, 643; *Paper Savers*, 51 Cal.App.4th at 1098; *Clement v. Smith* (1993) 16 Cal.App.4th 39, 45.

[16] *E.g., Murray v. UPS Capital Ins. Agency, Inc.* (2020) 54 Cal.App.5th 628, 639; *Fitzpatrick,* 57 Cal.App.4th at 922; *Desai*, 47 Cal.App.4th at 1119-1120; *Free*, 8 Cal.App.4th at 1729 *Jones v. Grewe* (1987) 189 Cal.App.3d 950.

[17] Also, good experts are essential. Insurance producers are a species of professionals, so any case involving allegations of professional negligence will require an expert to establish the standard of care and whether the conduct of the defendant(s) met that standard.

[18] Cal. Ins. Code §§ 700(c), 1631, 1633.

[19] Cal. Ins. Code §§ 1631, 1633, 1761, 1766.

[20] Cal. Ins. Code § 35.

[21] *Fraser-Yamor Agency, Inc. v. Cty. of Del Norte* (1977) 68 Cal.App.3d 201, 212–13.

[22] *Anserve Ins. Servs., Inc. v. Kelso* (2000) 83 Cal.App.4th 197, 206.

[23] 39 Op.Atty.Gen. 126, 2-27-62. (The only time an unlicensed person can issue a certificate of insurance in California is if the certificate is "under a running inland marine insurance contract," and even then, only if "no commission is paid or allowed [for] engaging in those activities." Cal. Ins. Code § 1635.)

[24] *Nowlon v. Koram Ins. Ctr., Inc.* (1991) 1 Cal.App.4th 1437.

[25] *E.g., R&B Auto Ctr., Inc. v. Farmers Group, Inc.* (2006) 140 Cal.App.4th 327, 337 (carrier can be held vicariously liable for misrepresentations by agent); *Desai*, 47 Cal.App.4th at 1120 (carrier can be held vicariously liable for misrepresentations by agent).

[26] *See*, CACI 2334 and notes.

[27] *Valentine v. Membrila Ins. Services, Inc.* (2004) 118 Cal.App.4th 462.

[28] *Prentice v. North Amer. Title Guar. Corp.* (1963) 59 Cal.2d 618, 620–621; *Sindell v. Gibson, Dunn & Crutcher* (1997) 54 Cal.App.4th 1457, 1470.

[29] *Third Eye Blind, Inc. v. Near North Entertainment Ins. Services, LLC* (2005) 127 Cal.App.4th 1311, 1324-1325. These can be reduced or offset to the client collects attorney fees from the insurer as bad faith damages. *See, e.g., Brandt v. Superior Court* (1985) 37 Cal.3d 813, 817.