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Insurance Marketer Malpractice

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All too often insurance companies justify a claim denial based on an allegation that there is no coverage. On other occasions, it appears that coverage adequate to fairly compensate an injured party is not readily available. Lawyers for insurance consumers are forced to search the policy for conflicting language and ambiguities in an effort to find adequate coverage. Remember, insurance companies write policies so that (1) the sales people can sell polices and (2) the claim people can deny claims. Coverage litigation is frequently lost on summary judgment because the insurer's attorneys are successful in persuading the judge to focus on conditions, limitations and exclusion that favor the insurance company. To counter this, lawyers attempt to plead and prove a case for "reasonable expectations" to get around difficult contract language. Such a case is sometimes difficult to prove and vulnerable to summary disposition.

If there is a claim denial based on a lack of coverage or apparently not enough coverage, attorneys for claimants must examine the role of the insurance marketer. What did the insurance consumer request? What did the marketer say to the consumer? Did the consumer request full coverage? Did the consumer ask that he or she be covered for "everything"? What did the sales literature imply? Did the insurance marketer boast of good service or peace of mind? What does the marketer's Web page say? Was the UM/UIM coverage less than the BI liability coverage in the policy?

A. Legal duty of an insurance marketer in Arizona.

The Arizona Supreme Court has established the legal duty of an insurance marketer in Arizona. Insurance marketers "owe a 'duty to the insured to exercise reasonable care, skill and diligence' in carrying out the duty to procure insurance." *Webb v. Gittlen*, 217, Ariz. 363, 369, 174 P.3d 275, 279 (2008), quoting *Darner Motor Sales, Inc. v. Universal Underwriters Ins. Co.*, 140 Ariz. 383, 397, 682 P.2d 388, 402 (1984).

B. Distinction between legal duty and standard of care.

It has been recognized that it is very easy for anyone to confuse the legal duty of an insurance marketer as set forth above with the standard of care that the marketer may owe to his or her client. The legal duty of an insurance marketer is always the same although the standard of care may change depending upon the circumstances and the facts presented. The distinction between the legal duty and the standard of care is discussed in *Southwest Auto Painting & Body Repair, Inc. v. Binsfield*, 183 Ariz. 44, 446-47, 904 P.2d 1268, 1270-71 (App. 1995):[2]

> The distinction between duty owed and breach of the standard of care long has been a source of confusion. The Arizona Supreme Court addressed the distinction in Markowitz v. Arizona Parks Board, 146 Ariz. 352, 706 P.2d 364 (1985), in which the court stated that "the existence of a duty is not to be confused with details of the standard of conduct." Id. at 355, 706 P.2d at 367. Duty is found in the relationship between individuals that "imposes upon one a legal obligation for the benefit of the other...." Id. (quoting W. PAGE KEETON ET AL., PROSSER AND KEETON ON THE LAW OF TORTS § 53, at 356 (5th ed. 1984)). Details of conduct, such as whether a defendant should have posted warning signs or fixed potholes, have to do with whether the defendant breached the applicable standard of care, not whether a duty and attendant standard of care exist. Id.; See also Coburn v. City of Tucson, 143 Ariz. 50, 52, 691 P.2d 1078, 1080 (1984).

In *Darner Motors Sales, Inc. v. Universal Underwriters Insurance Company, supra.*, (140 Ariz. at 398, 682 P.2d at 403) the Arizona Supreme Court stated: "The principle involved here is simply that a person who holds himself out to the public as possessing special knowledge, skill or expertise must perform his activities according to the standard of his profession. If he does not, he may be held liable under ordinary tort principles of negligence for the damage he causes by his failure to adhere to the standard." See W. Prosser, Law of Torts § 32, at 161-62 (4th Ed. 1971)." Proof of the standard in this type of case may require expert testimony at trial. [Footnote 4. We take note that Doxsee was not an independent agent, but was employed by Universal. We do not imply, by this opinion, that the standard of care is the same. It may be that "company agents" are held to a somewhat lower standard than "independent agents"; this, of course, is a matter of evidence."]

Justice Feldman mused that there may be a different standard of care for an independent producer than a direct producer, but he emphasized the fact that the duty is the same.

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The text of the opinion also emphasizes that fact that proof of a failure to adhere to a standard of care may be something that requires expert testimony.

C. What if the insurance marketer is not a licensed insurance producer?

Several years ago, the Arizona Legislature abolished the distinction between an insurance agent and an insurance broker and lumped them together as "insurance producers". A.R.S. § 20-281(5) defines an "insurance producer" as "a person required to be licensed under [the insurance code] to sell, solicit or negotiate insurance." Insurance companies themselves are not required to utilize the services of a licensed insurance producer to market their insurance. A.R.S. § 20-283(A) allows insurers to market insurance through its officers, directors, employees, subsidiaries, or affiliates.

D. Independent marketers, captive marketers and direct marketing.

The marketing of insurance is accomplished in three general ways. First, insurance is marketed through "independent" insurance producers who have written agreements with more than one insurance company. Second, insurers market their insurance contracts through "captive" producers under an agreement that requires the producer to sell exclusively or almost exclusively for one insurance company. Finally, insurance companies are allowed to market insurance on a "direct" basis without using licensed insurance producers. Examples of independent producers would be those who sell insurance for Hartford, Safeco, Chubb, or Liberty Mutual. Companies that market through captive producers include State Farm, Farmers, and American Family. Insurers who sell directly to consumers include Geico and USAA. The Trend is to market more insurance directly to the insurance buying public. Even independent insurers market directly in competition with their own independent producers.

E. Standard of care for insurance marketers.

In my opinion, the standard of care for an insurance marketer in Arizona requires that the marketer be knowledgeable and understand what her client's needs are and furnish information sufficient to allow the client a chance to make an informed decision about what risks he wants to insure. In some cases, the marketer must recommend and encourage purchasing coverage. Moreover, the standard of care requires an insurance marketer to have an understanding of what types of products are commercially available to consumers in Arizona and what they potentially cover. If the marketer does not do this, she cannot adequately inform the client about which risks to insure with what product.

In addition to the forgoing, the standard of care for insurance marketers in Arizona requires that insurance marketers engage in "field underwriting." This is process whereby the insurance marketers makes an inspection of the risk being insured and advises the insurance customer regarding several matters including the insurability of the risk, the coverages available for the risk and the amount of insurance that is recommended to be placed on the risk.

In the case of property insurance, the standard of care for insurance marketers is that the marketers advise the insurance customer in a manner that is clearly understood by the customer that the amount of insurance placed on the property risk should be as near as possible to the replacement cost of the property. The marketer should further carefully explain so that the insurance customer fully understands that the failure to have the property insured within a particular range (*i.e.:* 90%) of the replacement cost will result in a penalty being applied by the insurance company that will decrease the amount of indemnity that the insurance company is obligated if a claim arises. Obviously, insurance customers should be encouraged to insure the property for its full replacement value.

In the case of a liability risk (including a UM/UIM risk) the insurance marketer should review the insured's exposure to loss and tolerance for the retention of risk. UM/UIM coverage should always be recommended at limits that are the same as the BI liability limits.[3]

F. Let the Jury decide insurance marketer malpractice.

Because the legal duty imposed on insurance marketer is so clearly stated in the case law, a trial court judge's hands are tied. If the attorney for the injured party brings a claim for insurance marketer malpractice and supports it with expert testimony defining the standard of care, violation of the standard of care and causation, damages almost always take care of themselves. That is, damages are usually defined by the loss for which the insurance company has denied coverage. In other words, a trial lawyer is probably going to be able to get her or his client's case before a jury.

One thing that the insured and each member of the jury have in common is that none of them fully understand the insurance transaction and rely on their insurance marketer and insurer to guide them to make a prudent decision.

G. Don't forget to disclose your expert insurance witness in the claim against a "licensed professional."

A.R.S. § 12-2602 requires that certain disclosures be made when bringing a civil action against a licensed professional. Insurance producers, of course, are licensed professionals like doctors, lawyers and architects.

When presenting your claim, A.R.S. § 12-2602(A) requires that you "certify in a written statement that if filed and served with the claim" whether expert opinion testimony is necessary to prove a license professional's standard of care or liability. If so certified, A.R.S. § 12-2602(B) requires you to serve a preliminary expert opinion affidavit with your Initial Disclosure Statement under Rule 26.1 A.R.C.P. This preliminary affidavit must include the following:

- The expert's qualifications to express an opinion on the licensed professional's standard of care or liability for the claim.
- The factual basis for each claim against a licensed professional.
- The licensed professional's acts, errors or omissions that the expert considers to be a violation of the applicable standard of care resulting in liability.
- The manner in which the licensed professional's acts, errors or omissions caused or contributed to the damages or other relief sought by the claimant.

H. Consider accepting an assignment of a claim for insurance marketer malpractice or suing the insurance marketer for breach of contract to procure insurance.

In *Webb v. Gittlen*, 217, Ariz. 363, 369, 174 P.3d 275, 279 (2008), the Arizona Supreme Court introduced, for the very first time, the ability of an insured to assign a tort claim for insurance marketer malpractice to an injured party in connection with a settlement of a claim. This had previously prohibited in *Premium Cigar Intl, Ltd. v. Farmer-Butler-Levitt Insurance Agency,* 208 Ariz. 557, 96 P.3d 555 (App. 2004). This change opens the door for a claimant to consider taking up the challenge of proceeding with an insurance marketing malpractice claim in lieu of the dim prospect of attempting recovery from a party who is not financially responsible. Such "*Webb* Agreements" are only beginning to be used as their availability becomes more widely known among trial lawyers.

When an insurance marketer fails to place coverage requested by a customer, the

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marketer can be found guilty of breach of contract to procure insurance. This is a case of action sounding in contract which opens up two doors. First, the claim allows the prevailing party to seek reasonable attorney's fees pursuant to A.R.S. § 12-341.01 (albeit a two-edged sword). Second, it establishes the ability of an insured third party to accept an assignment of a cause of action from an insured under a "*Premium Cigar* agreement."

Lawyers should carefully review *Premium Cigar Intl, Ltd. v. Farmer-Butler-Levitt Insurance Agency,* 208 Ariz. 557, 96 P.3d 555 (App. 2004).[4] If there is a "specific promise" to procure insurance, the cause of action sounds in contract and may be assigned like any other contract claim. (208 Ariz. at 568-69, 96 P.3d at 566-57).

I. Case Studies.

1. UM/UIM

There is hardly ever a justified explanation for an insurance consumer purchasing UM/UIM coverage that does not parallel the bodily injury liability coverage. Take the case of Dr. C who was very loyal to his insurance company, Great Benefit Auto Insurance Company. It seems that Dr. C first purchased low limits auto insurance when he was in the Air Force because Great Benefit, a direct writer, had an office very near the main entrance to the base. At renewal time, Dr. C was presented a menu of coverages and was given the opportunity to check off changes in his automobile insurance policy. He gradually moved his primary BI limit to $1 million dollars and also purchased a $1 million dollar umbrella policy. All this time, however, his UM/UIM insurance remained at $15/$30.

Unfortunately, Dr. C was involved in a horrendous car crash with an underinsured motorist.

After the claim was presented to Great Benefit Auto, Great Benefit promptly dispatched to Dr. C its draft for $15,000.00 but insisted that he complete UM/UIM release be signed. Dr. C hesitated and went to visit a member of the Arizona Trial Lawyers Association. Suit was filed against Great Benefit Auto for insurance marketing malpractice, bad faith claim handling and punitive damages. Soon after disclosure statements were exchanged, the litigation was settled.

(In a previous case, Great Benefit Auto had persuaded a trial court judge to grant its summary judgment for malpractice under the theory that because the telephone operators at Great Benefit Auto are not required to be licensed as insurance producers in Arizona, Great Benefit Auto does not owe any duty of care to the insurance buying public of Arizona. The Arizona Court of Appeals reversed this preposterous argument and remanded the matter for trial on the insurance producer malpractice theory. Unfortunately, the decision of the Arizona Court of Appeals only appeared as a memorandum decision. (This hypothetical case study is not unlike what occurred in *Lesser v. U.S.A.A.*, No. 1CA-CV00-0453]).

2. Furniture City v. Great Benefit Property Insurance Company

Furniture City is a warehouse style retail furniture store located in a smaller Arizona city. It was continuously owned by the same family for two generations. Every few years, the business owners put the property and liability insurance "out to bid" to see if "better" premium was available. At renewal, Pearless Insurance Agency came in with a low bid based upon duplicating coverages in the prior policy that was originally written many years ago.

Unfortunately, a fire occurred that completely destroyed the entire structure and all of its contents. When the claim was presented, Great Benefit Property Insurance Company informed the unhappy insured that the building was only insured for $1 million dollars and that it would cost about $5 million dollars to replace the structure. The contents were similarly underinsured.

Because of the application of a 90% co-insurance clause, the insured was supposed to insure the property to at least 90% of its replacement value ($4,500,000) an 88% co-insurance penalty resulted in insurance coverage on the structure being reduced to $220,000. A similar co-insurance penalty applied to the contents loss.

Furniture City sued its insurance agency for insurance marketer malpractice and settled for damages equal to what the property should have been insured for.

3. No proper coverage.

Southwest Auto Painting and Auto Repair, Inc. purchased from Jay Binsfield at General Southwest Insurance Agency, Inc. Unfortunately, Mr. Binsfield did not mention that employee dishonesty coverage could have been easily included on the business policy. This omission was not discovered until after an employee of Southwest was discovered to have embezzled significant funds. The insurance company denied any liability and a malpractice action was brought against the insurance agency.

Southwest's insurance standard of care expert (yours truly) testified at deposition presented to the trial court in connection with the defense of a Motion for Summary Judgment that the standard of care required the insurance producer to advise the insured about the relevant types of coverage that are available and the costs of such coverage. The insurance expert also offered his opinion "that, because fidelity coverage is widely available at a relatively modest cost, insurance agents should recommend it to businesses that have employees outside the owner's family who either have check-signing authority or handle cash." Unfortunately, the Maricopa County Trial Court granted summary judgment but the Court of Appeals reversed holding that this testimony raised a question of fact as to whether the standard of care for an insurance marketer such as Binsfield includes the responsibility to advise a client of the availability of relevant types of coverage. *Southwest Auto Painting & Body Repair, Inc. v. Binsfield*, 183 Ariz. 444, 904 P.2d 1268 (App. 1995).

4. A v. Great Benefit Life Insurance Company

Mrs. A was very interested in getting some life insurance covering her husband who worked in a blue collar occupation without benefits. She called up Great Benefit Life Insurance Company to set up an appointment so that its agent, Ima Eager to visit Mrs. A at her kitchen table. It seems that the insurance producer had never actually assisted a customer to fill out an application before and wrote down Mrs. A's date of birth for that of her insured husband. Since Mrs. A was about five (5) years older than her husband, the underwriters at Great Benefit Life Insurance Company wanted Mr. A to undergo a paramedical examination and provide fluid samples. Great Benefit Life, however, never communicated its desire for such a medical test to either Mr. A or Mrs. A and had difficulty in getting either one of them on the telephone. The insurance agent was aware of this difficulty so she reduced the amount of insurance applied for from $150,000 to $100,000 on the strength of a forged signature on a change form so that the company would no longer be interested in obtaining a fluid sample. Great Benefit Life Insurance Company never informed Mr. or Mrs. A that a life insurance evidenced by a binder was not in force.

Mr. A unexpectedly died of a heart attack and Mrs. A presented a death claim. Great Benefit Life Insurance Company, of course, undertook a comprehensive post loss underwriting review and concluded that there were several things on the application of insurance that were not true. Unfortunately, neither Mr. nor Mrs. A had an opportunity to review the health questions asked during the application process because they were never given a copy of this portion of the application. A.R.S. § 20-1108 provides that no part

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of an application for life or disability insurance is admissible into evidence unless it is provided to the insurance consumer.

J. Conclusion.

When a party is advised that the claim is not covered or is underinsured, the attorney for the claimant must consider making a claim for insurance marketer malpractice (a tort claim) and breach of contract to procure insurance (a contract claim). Juries are quick to appreciate the complexity of the insurance transaction as well as the insurance marketer's role in the process of procuring coverage. Individual jurors rely upon the expertise and advice of their insurance marketer and easily understand that insurance marketers are professionals just like doctors or lawyers. Since the insurance company usually takes a firm position of no coverage, the lawyer can often enlist the expertise and power of the insurance company in presenting a claim against an insurance marketer.

The trend in America is for insurance to not be produced by independent agents in the American Agency System. Rather, more and more insurance is produced on a direct basis by the insurance company. It makes no difference whether the insurance marketer is independent, captive or a direct employee of the company. It makes no difference if the producer is a nameless person on the other end of a toll free telephone, an internet screen, or even a gecko. The legal duty owed by all insurance marketers is the same. If the jury is presented probative evidence supporting the insurance marketer's violation of the standard of care, evidence of causation and damages, a claimant can reasonably expect substantial justice. ■

Endnotes

1 Rick Berry earned his Bachelor of Science degree in Insurance (1969) and a Juris Doctor degree (1973) from Arizona State University. He served as the Deputy Director of Insurance of the State of Arizona from July 1, 1976 through September 30, 1978 and attained the professional insurance designations of Charter Property and Casualty Underwriter (CPCU) in 1981 and Chartered Life Underwriter (CLU) in 1983. He served as a member of the State Bar Insurance Committee for many years and as Chairman of that Committee for a number of years. Rick is a licensed insurance producer in Arizona for life, health, disability, property and liability insurance. Attached is a copy of my curriculum vitae which lists his publications. These publications can be viewed by links provided in my webpage, www.azinsurancelawyer.com.

2 The author was the insurance expert witness for the insured.

3 The only reasonable exception for not following this standard of care is where the insured requests only minimum financial responsibility limits and buys no more than an auto policy with only the minimum limit (i.e., no coverage for collision, comprehensive, medical payments, towing, mechanical breakdown, or any other risk of loss).

4 The author was the insurance expert witness for the insurer.given a copy of this portion of the application. A.R.S. § 20-1108 provides that no part of an application for life or disability insurance is admissible into evidence unless it is provided to the insurance consumer.

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On 1-4-2012, the 3rd Circuit unanimously denied US Airway's Petition for rehearing en banc in this case. It is expected that the ERISA plan will file a Petition for Writ of Cert in the U.S. Supreme Court.

Meanwhile in our Ninth Circuit, similar issues have been heard in CGI v. Rose, Nos. 11-35127, oral argument having been heard on 2-9-2012, with a decision expected in coming months. I am hopeful that the Ninth Circuit will follow the lead of the Third Circuit in McCutcheon. ■