

TO WHOM IS A DUTY OWED: THE DUTIES OF CAPTIVE INSURANCE AGENTS, BY: DONALD PATRICK ECKLER, ESQ., AND BRIDGET CHOI, ESQ.

Often controlled by statute, the duties owed by captive agents to insureds vary across the country. With a recent decision from the Illinois Supreme Court, the definitions of “producer,” “agent,” and “broker” will continue to be blurred and duties that are owed and to whom those duties are owed will likely expand.

The *Skaperdas* Decision

In *Skaperdas v. Country Casualty Insurance Co.*, Country Casualty, by its agent Tom Lessaris, issued an automobile insurance policy to the one of the plaintiffs, Steven Skaperdas. *Skaperdas v. Country Casualty Insurance Co.*, 2015 IL 117021, ¶ 4. Following an accident in which Skaperdas’s fiancé, Valerie Day, was injured while driving one her fiancé’s vehicles, Country Casualty required Skaperdas to amend his policy to include Day as an additional driver. *Id.* Skaperdas met with Lessaris to change the policy. *Id.* Lessaris prepared the policy, but only identified Skaperdas as the named insured, and identified the driver as a “female, 30-64.” *Id.* Subsequently, Day’s minor son, Jonathon Jackson, was struck by a vehicle while riding his bicycle. *Id.* at ¶ 5. The driver’s policy limit was insufficient to cover Jackson’s injuries, so Skaperdas and Day made a claim for underinsured motorist benefits under the policy. *Id.* Country Casualty denied the claim on the basis that neither Day nor Jackson was listed as a named insured. *Id.*

Skaperdas and Day filed a complaint alleging, *inter alia*, that Lessaris was negligent in failing to obtain the insurance as requested by Skaperdas. *Id.* at ¶ 6. Specifically, they alleged that Lessaris breached his duty to exercise ordinary care in renewing, procuring, binding, and placing the requested insurance coverage as provided by section 2-2201 of the Code of Civil Procedure. *Id.* In relevant part Section 2-2201 states:

An insurance producer, registered firm, and limited insurance representative shall exercise ordinary care and skill in renewing, procuring, binding, or placing the coverage requested by the insured or proposed insured.

No cause of action brought by any person or entity against any insurance producer, registered firm, or limited insurance representative concerning the sale, placement, procurement, renewal, binding, cancellation of, or failure to procure any policy of insurance shall subject the insurance producer, registered firm, or limited insurance representative to civil liability under

standards governing the conduct of a fiduciary or a fiduciary relationship except when the conduct upon which the cause of action is based involves the wrongful retention or misappropriation by the insurance producer, registered firm, or limited insurance representative of any money that was received as premiums, as a premium deposit, or as payment of a claim.

The provisions of this Section are not meant to impair or invalidate any of the terms or conditions of a contractual agreement between an insurance producer, registered firm, or limited insurance representative and a company that has authority to transact the kinds of insurance defined in Class 1 or clause (a), (b), (c), (d), (e), (f), (h), (i), or (k) of Class 2 of Section 4 of the Illinois Insurance Code.

While limiting the scope of liability of an insurance producer, registered firm, or limited insurance representative under standards governing the conduct of a fiduciary or a fiduciary relationship, the provisions of this Section do not limit or release an insurance producer, registered firm, or limited insurance representative from liability for negligence concerning the sale, placement, procurement, renewal, binding, cancellation of, or failure to procure any policy of insurance.

Lessaris moved to dismiss the negligence claim, arguing that he did not owe the plaintiffs a duty of care in procuring coverage. *Id.* at ¶ 7.

Holding of Trial and Appellate Court

The circuit court agreed, and granted the motion to dismiss the negligence count. *Id.* at ¶ 8. The appellate court, however, reversed, holding that a plain reading of section 2-2201 along with the definition of “insurance producer” set forth in section 500-10 of the Illinois Insurance Code, established that “any person required to be licensed to sell, solicit, or negotiate insurance has a duty to exercise ordinary care in procuring insurance.” *Id.* at ¶ 9 (internal citations omitted).

Holding of Illinois Supreme Court

On appeal to the Illinois Supreme Court, Lessaris argued that section 2-2201 does not impose a duty of ordinary care on a “captive insurance agent” with regard to procuring insurance for a client. *Id.* at ¶ 12. Rather, he argued, a captive insurance agent is one who owes a duty to the company who employs him, not the insured, and that only insurance brokers, because they are employed by the insured, owe a fiduciary duty to the insured. *Id.* Section 2-2201 was intended to limit the liability of

insurance brokers in a fiduciary relationship, and as an insurance agent, he did not owe a duty to the plaintiffs. *Id.*

Considering Lessaris' arguments, the Court turned to the statute. Section 2-2201 provides in relevant part that "[a]n insurance producer, registered firm, and limited insurance representative shall exercise ordinary care and skill in renewing, procuring, binding, or placing the coverage requested by the insured or proposed insured." *Id.* at ¶ 17, citing 735 ILCS 5/2-2201(a). The Court noted that the term "insurance producer" was not defined in section 2-2201. *Id.* at ¶ 18. It further noted while that insurance law distinguishes between insurance agents and brokers, it does not address whether insurance agents, brokers, or both could be classified as an "insurance producer." *Id.* at ¶ 19. The Court further observed that Black's Law Dictionary included the term "producer" in both the definition of an "insurance agent" and an "insurance broker." *Id.* at 20. Thus, finding the statute to be ambiguous as to the term "insurance producer," the Court turned to extrinsic aids of construction. *Id.* at ¶¶ 27-28.

The Court began by examining the definition of "insurance producer" in section 500-10 of the Insurance Code which defines an insurance producer as "a person required to be licensed under the law of the State to sell, solicit, or negotiate insurance." *Id.* at ¶ 29, citing 215 ILCS 5/500-10. Although the defendants argued that the Insurance Code was inapplicable because it was not part of the Code of Civil Procedure, the Court observed that section 2-2201 expressly refers to the Insurance Code, recognizing a connection between the two provisions. It also acknowledged that the legislature was aware of section 2-2201 when it enacted the definition of "insurance producer" when the Insurance Code became effective in 2002. *Id.* at ¶ 30. The Court further examined the legislative history of section 2-2201 and found that the term "insurance agent" was consistently used with no distinction between agents and brokers. *Id.* at ¶¶ 31-33.

Finally, the Court also observed that Illinois courts have previously recognized that a captive agent *may* owe a duty to an insured in certain situations. *Id.* at ¶ 35. For example, in *Talbot v. Country Life Ins. Co.*, 8 Ill. App. 3d, 1062 (3d Dist. 1973), the Third District appellate court held that an agent has a duty of care such he or she may be liable for unreasonably delaying an application for life insurance. *Id.* More recently, in *Bovan v. American Fam. Life Ins. Co.*, 386 Ill. App. 3d 933 (1st Dist. 2008), the First District affirmed that a captive insurance agent may owe a proposed insured a duty of ordinary care in some circumstances, though it declined to find such circumstances existed based on the facts at hand. *Id.*

On these grounds the Court concluded that "the best evidence of the legislature's intent in using the term "insurance producer" [was] the statutory definition in section 500-10 of the Insurance Code." *Id.* at ¶ 43. In light

of that definition, section 2-2201 mandates that a person who is required to be licensed to sell insurance has a duty to exercise ordinary care and skill in the renewing, procuring, binding, or placing of coverage as requested by the client. *Id.* As a result, the Court concluded that section 2-2201 imposed a duty of ordinary care on Lessaris even as a captive insurance agent to procure the coverage requested by Skaperdas and Day. *Id.* at ¶ 45.

Producer, Agent, and Broker Outside of Illinois

As is clear from *Skaperdas* decision the term "producer" as used in section 2-2201 of the Illinois Code of Civil Procedure refers to both agents and brokers, whether captive or independent. More generally however, a producer who represents the insurers is referred to as an agent and a producer who represents insureds is referred to as a broker. *Agent Misconduct*, DRI Life, Health, Disability, and ERISA Claims Seminar, Leonor Lagomasino, April 2009. Under that definition, Lessaris was an agent. An insurer is generally vicariously liable for acts of its agent, whereas the insured is liable for the acts of his broker. Sometimes, as in the case in Illinois, a producer can be a dual agent. 4 *Couch on Insurance*, § 45.1 (3d ed. 20).

What a producer is called is not determinative of the status of the producer or to whom duties are owed by the producer. In *Benante v. United Pac. Life Ins. Co.*, 659 N.E. 2d 545, 548 (Ind. 1995), the Supreme Court of Indiana set forth some of the factors to consider in determining the duties owed:

- the relation of the parties, their actions, and usual course of dealing;
- instructions given to the producer by the insurer;
- whether one party can control the actions of the producer;
- parties' conduct generally; and
- the nature of the transaction.

Liability of Captive Agents

The general rule in California, which is obviously different from Illinois law, is that "an insurance agent whose principal is disclosed cannot be held individually liable to an insured." *Limm v. George J. Hahn*, 2006 U.S. Dist. LEXIS 58894, *5 (E.D. Cal. Aug. 18, 2006) citing *Quiroz v. Valley Forge Ins. Co.*, 2005 U.S. Dist. LEXIS 43316, *13 (N.D. Cal. July 25, 2005); see also *Lippert v. Bailey*, 241 Cal. App. 2d 376, 382 (4th Dist. 1966). There are two exceptions to this rule, the dual agency exception and the "special duty" exception. The dual agency exception applies where the client is unaware of the relationship between the agent and the carrier. *Lippert*, 241 Cal. App. at 383. That circumstance would rarely apply, and certainly did not apply in the circumstances of the *Skaperdas* case.

California's "special duty" exception applies in a far broader set of circumstances that often will obtain when dealing with a captive agent:

- (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 agent 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. *Fitzpatrick v. Hayes*, 57 Cal. App. 4th 916, 926-927 (1st Dist. 1997).

These exceptions too, would not apply to the situation in *Skarpedas*.

Finally, a captive agent can also be individually liable under California law to an insured under the "special duty" exception when the agent promises to procure insurance for the insured but fails to do so because an insurance agent has an obligation to use reasonable care, diligence, and judgment in procuring the insurance requested by an insured." *Butcher v. Truck Ins. Exch.*, 77 Cal. App. 4th 1442, 1461 (2nd Dist. 2000). This is what the individual defendant in *Skarpedas* is alleged to have done. Accordingly, even in a state with such a general rule as California that a captive agent whose principal is disclosed is not individually liable, liability can clearly be possible.

***Skarpedas* is a Harbinger of the Tough Legal Battles Ahead for Captive Insurance Agents**

Finding that a duty to exercise ordinary care may be applied to any insurance salesperson regardless of whether a fiduciary or agency relationship obtains, applies a new duty to captive agents and perhaps one that may conflict with their duties to the insurer who employs the agent. (Complicating things in Illinois is the fact that a producer owes no fiduciary duties to the insured except in the handling of money for the insured. 735 ILCS 5/2-2201(b); *Melrose Park Sundries, Inc. v. Carlini*, 399 Ill. App. 3d 915, 921 (1st Dist. 2010)). Captive agents are bound by their contractually agreed upon duties to the carrier. *Skarpedas* burdens the captive agent with duties to both its principal and the person seeking insurance. When those two duties are at conflict with each other the captive agent could be in an untenable situation and both the insured and the captive agent would likely suffer.

Using the facts of *Skarpedas* as an example, depending on the terms of the agency contract, captive agents could find themselves liable to the insurer for expenses and costs it expends in a declaratory judgment action filed to resolve coverage issues. If the agency agreement obliges the agent to exercise ordinary care and skill in the renewing, procuring, binding, or placing of coverage and a mistake is

made that causes the carrier to be sued, the carrier could pursue the agent for the breach of contract damages it caused in failing to properly bind the coverage. Then, the captive agent could allegedly be liable to both the policyholder and the company for the same act or omissions.

Practical Applications

First, it will be ever more important for captive agents to review the language of the agency agreement in evaluating their risks and in determining what action (or inaction) they should take in particular situation.

Second, captive agents should consider purchasing policies of insurance to insure them for the unique set of risks that they face. Currently, many captive agents do not have such coverage as they have deemed it unnecessary, but in light of this development in the law, such coverage is indeed necessary.

Third, captive agents, who now may owe duties to two masters, cannot favor one principal over another. Disclosure, communication, and well documented files will be essential to defend against claims. This is no different than what other professionals have been advised to do for a long time, but captive agents have always had clearly defined duties going in one direction owed to among the most sophisticated of principals, an insurer, who was their employer. That is no longer the case, as a captive agent now owes duties to an unsophisticated individual with limited understanding of insurance. Documenting the communications and advice to the insured and the directions received from the insured will be critical.

In short, the *Skarpedas* decision portends a whole new set of challenges for captive agents that will require diligence to manage, handle, and defend against.



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