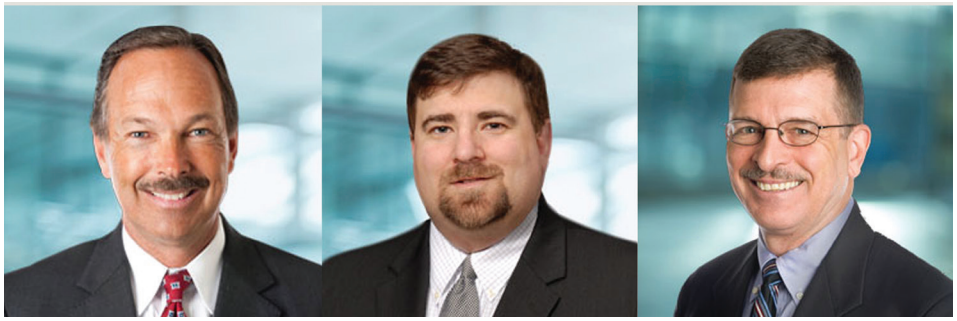
The Legal Intelligencer
THE OLDEST LAW JOURNAL IN THE UNITED STATES 1843-2021
PHILADELPHIA, MONDAY, JULY 26, 2021
An ALM Publication

Are Insurance Brokers the Next Target for Claims Arising From the Pandemic?

BY MICHAEL KASSAK, CHRISTOPHER LEISE AND MARC PENCHANSKY



Courtesy photos

L-R: Michael O. Kassak, Marc Penchansky, and Christopher P. Leise of White and Williams.

Since the pandemic struck last March, policyholders have sued insurance carriers nearly **2,000 times alleging their policies covered business losses due to COVID-19** and the related civil authority orders. These claims have primarily focused on business-interruption coverage with policyholders seeking reimbursement for lost income due to pandemic-related mandatory closures orders. COVID-19-related claims have also arisen under event cancellation, directors and officer's liability and general liability policies. Other types of claims may also be around the corner. For example, employers' responses to the pandemic increased their vulnerability to cyberattacks resulting in additional exposure to brokers for claims by policyholders who do not have cyber-specific insurance coverage.

While some policyholders have sued their brokers for COVID-19-related coverage gaps, our research suggests there have been few cases. This is not surprising, because policyholders often wait to pursue errors and omissions claims until they exhaust efforts to pursue coverage, and policyholders' counsel are likely awaiting the outcome of coverage suits before pursuing brokers. If courts continue to find—as they have in most cases—that industry-standard property policies do not cover COVID-19-related losses, policyholders might turn to their brokers and argue for liability flowing from the broker-client relationship. Clients might contend that additional endorsements or coverage forms should have been offered. To the extent that courts conclude that the direct physical loss requirement is satisfied but the claim is excluded due to the presence of a virus exclusion, policyholders might also contend brokers should have provided quotations without the virus exclusions. Finally, to the extent coverage would have been available but brokers did not submit a claim to the insurers, brokers might face claims of negligent claims handling.

Recently, the U.S. Court of Appeals for the Eighth Circuit was the first appellate court to weigh in on the issue of coverage for business income lost due to COVID-19. It held that the insured failed to state a breach-of-contract claim because no nexus existed between a physical loss, as required by the policy, and lost business income. See *Oral Surgeons v. Cincinnati Insurance*, No. 20-3211, 2021 U.S. App. LEXIS 19775 (8th Cir. July 2, 2021). Now that appellate courts have started to opine on coverage under commercial property

policies, this is a good time to consider insurance brokers' potential liability for business-interruption claims and cyber claims.

- **Brokers Have No General Duty to Advise Clients to Protect Themselves from Virus-Related Losses**

When determining whether a broker breached a duty while soliciting, quoting, and binding coverage, the threshold question is whether the state treats a broker as an order taker or an advisor with heightened duties to assess exposures and make recommendations about a client's needs. In some states like Texas and New York, courts focus on the transaction and identify the duty with an assist from contract law. *See*, *Sonic Systems International v. Croix*, 278 S.W.3d 377, 394 (Tex. App. 2008); *M&E Manufacturing v. Frank H. Reis,* 692 N.Y.S. 2d 191, 193 (App. Div. 1999). In those states, a policyholder will find it difficult to hold its broker liable for failing to provide business-interruption coverage without an explicit client request to do so.

Other states focus on the broker-client relationship and require a broker to act with reasonable skill and diligence. See *Rider v. Lynch*, 42 N.J. 465, 476, (1964). In these states, a broker may be liable when it neglects to procure insurance, fails to follow the client's instructions, or if the policy is void or materially defective due to the broker's actions or omissions. See *Laventhol & Horwath v. Dependable Insurance Associates*, 579 A.2d 388, 391 (Pa. Super. 1990); *President v. Jenkins*, 180 N.J. 550, 569 (2004).

Brokers have fared well in the early cases filed against them. See *Wilson v. Hartford Casualty,* 492 F. Supp. 3d 417 (E.D. Pa. 2020); *Vandelay Hospital Group v. Cincinnati Insurance,* Civil Action No. 3:20-CV-1348-D, 2020 U.S. Dist. LEXIS 149196 (N.D. Tex. Aug. 18, 2020). However, the failure to act diligently regarding a client's COVID-19 concerns was the reason a Louisiana federal judge held that a policyholder stated a viable claim against its broker. In *B&P Restaurant Group v. Eagan Insurance Agency*, 2021 U.S. Dist. LEXIS 88330 (E.D. La. May 10, 2021), the client began renewal discussions with its broker in late 2019 during initial news reports about COVID-19's impact overseas. The client claimed it told the broker that a virus-related shutdown would devastate its business. In response, the broker allegedly explained the policy's civil-authority provision would cover any shutdown due to a government order. Furthermore, the broker allegedly did not advise its client that the proposed renewal policy had a virus exclusion or that the client could purchase virus coverage. Because of the broker's advice, the client renewed its policy with increased business-interruption limits. The court held that the broker might have breached its duty of reasonable diligence if it provided an inaccurate answer to the client's questions about the scope of available civil-authority coverage.

We anticipate that courts are unlikely to find a broker liable if it places a policy that uses the widely distributed form authored by the Insurance Services Office (ISO) or any similar forms which predicate coverage on "physical loss or damage" or which exclude virus-related losses. After all, policies with standard forms that include these terms are sold across the country. It is widely understood that this pandemic is the first of its kind for close to 100 years. Duties of professional liability are customarily formulated based on foreseeability, not hindsight. It is unlikely brokers would be held liable for failing to foresee the pandemic.

However, the defenses which accrue in a standard broker-client relationship might not apply when the broker and the client have formed a special relationship. A special relationship can arise when the broker acts more like a risk manager, when coverage is specifically requested by the insured, or if the broker engaged in a specific undertaking to procure coverage for a specific cause of loss. For example, a hospitality client who has long relied on its broker to assess risks to its business may viably claim that a broker was liable for not securing an endorsement with its event-cancellation insurance that covers virus-related cancellations.

Nevertheless, courts have consistently recognized that a commercial policyholder is in a much better position than its broker to know the potential risks to its business. See *Murphy*

v. Kuhn, 682 N.E.2d 972, 976 (N.Y. 1997). Imposing on brokers a general duty to advise about available coverages and other issues would remove from the insureds the burden to care for their own insurance needs and would permit insureds to seek retroactive coverage by claiming they would have bought additional coverage if offered by the broker. See *Nelson v. Davidson*, 456 N.W.2d 343, 367 (Wis. 1990).

• Brokers Should Advise Clients About the Availability of Cyber Coverage

While brokers are not risk managers, part of their job is to understand how trends affect coverage. A less obvious risk associated with COVID-19 is an increased vulnerability to a company's cybersecurity. The dramatic increase in remote employees was met with a significant increase in online activity seeking to breach security through phishing and similar schemes many of which were designed to exploit COVID-19 fears. Ransomware claims have dominated the news and are running rampant. Meanwhile, remote-working employees are more likely to forego best practices such as using personal devices without adequate security protections or failing to use secured lines while IT support is stretched thin due to the demands of COVID-19.

While coverage for privacy breaches, security lapses, and other cyber incidents is available in the marketplace, many businesses still do not purchase cyber coverage. When experiencing a cyber breach, these companies often make a "silent cyber" claim which arises when coverage is sought for cyber-related losses under policies not designed or rated to cover those losses. In other words, coverage for cyber losses is neither specifically included nor excluded under these policies.

If these silent cyber claims are unsuccessful—as they are likely to be—brokers may face claims for not explaining the availability of the coverage or not advising a client to procure the protection. Like with more traditional COVID-19-related claims, a key question will be whether the broker alerted the client to the availability of cyber coverage. If that duty is fulfilled, most states will only require a broker to do more if the client instructs it to do so. In a typical arms'-length broker-client relationship, advising of the availability of cyber coverage will be sufficient. Caselaw generally does not require a broker to recommend or purchase the additional protection. Because we anticipate that policyholders will continue to make claims, it is recommended that brokers review policy language with any client with concerns about the breadth of its cyber coverage.

Conclusion

Although policyholders have filed only a handful of COVID-19-related lawsuits against brokers, brokers should assume they are coming as clients look to recoup their COVID-19 losses. Assuming an arms'-length relationship, a written offer, and clear evidence of a business accepting the offer, we anticipate that brokers will mount strong defenses to any such claims. But it remains to be seen whether the courts will find that brokers who have undertaken some risk-management or advisory role with their clients will be found to have a duty to the client to anticipate the need for coverage for losses for a once-in-a-century pandemic.

***Michael Kassak**, a partner with White and Williams, has more than 30 years of experience as lead counsel litigating large complex commercial matters including cutting edge insurance coverage and healthcare disputes.*

***Christopher Leise**, senior counsel at the firm, focuses his practice on complex insurance and commercial litigation, including the representation of licensed insurance agents and brokers in professional liability claims and agency contract disputes.*

***Marc Penchansky**, counsel with the firm, has a varied practice with a focus on insurance coverage and related litigation, class actions, insurance broker and agent liability, medical malpractice, and appeals.*