



# GOLDBERG SEGALLA <sup>LLP</sup>

## PROFESSIONAL LIABILITY MONTHLY

A national professional liability newsletter

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*Professional Liability Monthly* provides a timely summary of decisions from across the country concerning professional liability policies. The publication is distributed monthly via e-mail. Cases are organized by topic, and where available, hyperlinks are included providing recipients with direct access to the full decision. In addition, we provide the latest information regarding news in the professional liability industry. We appreciate your interest in our publication, and welcome your feedback. We also encourage you to share the publication with your colleagues. If others in your organization are interested in receiving the publication, if you wish to receive it by regular mail or if you would like to be removed from the distribution list, please contact [Brian R. Biggie](#).

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A monthly summary of decisions affecting the insurance/reinsurance industry. For more information contact Jeffrey L. Kingsley at [jkingsley@goldbergsegalla.com](mailto:jkingsley@goldbergsegalla.com).

#### **CaseWatch**

A bi-weekly summary of appellate decisions concerning insurance law from across the country. For more information contact Sarah Delaney at [sdelaney@goldbergsegalla.com](mailto:sdelaney@goldbergsegalla.com).

#### **Insurance and Reinsurance Report**

Our [blog](#) featuring daily updates of world-wide decisions, developments and news affecting the global insurance industry.

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## I. Directors and Officers

### **WARREN v. FEDERAL INS. CO.**

(6<sup>th</sup> Cir. Dec. 22, 2009)

#### ***Bank's Statement That It Was "Evaluating" Its Rights Was Not A Claim***

Plaintiffs owned an interest in a series of companies, including Prime Measurement Products, LLC. Prime Measurement was a manufacturer of measurement tools and control sensors for oil, gas, and process markets. Plaintiff signed a personal guaranty on a line of credit extended by PNC Bank to Prime Measurement. The personal guaranty contained a "cognovit" provision which allowed the bank to enter a judicial confession of judgment.

After plaintiffs sold their interest in the company, it began experiencing financial difficulties. PNC Bank demanded that plaintiffs fulfill their obligations under the personal guaranty. Plaintiffs refused, and PNC Bank filed a complaint based upon the personal guaranty signed by both plaintiffs. However, the complaint did not allege any misrepresentations or improper conduct on the part of the plaintiffs.

On March 22, 2006, plaintiffs' attorney received a letter from PNC Bank concerning the guaranty and also stating that PNC Bank believed plaintiffs misrepresented the company's financial stability. In response to this letter, Prime Measurement notified Federal Insurance of the potential claim. Federal denied coverage under the directors and officers policy claiming the policy did not cover the "cognovit" guaranty raised in the PNC Bank complaint.

After a settlement was reached between plaintiffs and PNC Bank, plaintiffs filed suit against Federal Insurance asserting breach of contract and bad faith. The plaintiffs argued that the March 22, 2006 letter constituted a written demand for monetary damages and triggered coverage. Federal countered that the letter stated only that PNC Bank was evaluating its options and did not make a demand for monetary damages. The court agreed, noting that plaintiffs failed to cite any case law substantiating their assertion that PNC's letter was tantamount to a claim for monetary damages.

Moreover, the court went on to note that it was in the interests of both the plaintiffs and PNC Bank to set up Federal Insurance as the source of payment for the suretyship obligation, and the settlement agreement reflected that joint interest. Accordingly, the court stated that in such a situation, it is proper to require strict compliance with the insurance contract before shifting the payment obligation to the insurance company.

Finally, the court held that because plaintiffs were not entitled to coverage, the bad faith claim was properly dismissed.

**Impact:** Courts continue the exercise of interpreting the term "claim" narrowly in the context of professional liability policies. Here, the letter from PNC Bank simply indicated that it was evaluating its options. Interestingly, the court expressly commented on the parties' interest in construing the case in a way to trigger coverage. Accordingly, the court (properly) applied a strict interpretation of the policy.

For a copy of this decision, click here: <http://tinyurl.com/GS-PLM-Jan-15>

## II. Errors and Omissions

### **ENDURANCE AMERICAN SPECIALTY INS. CO. v. BOWEN, MICLETTE & BRITT, INC.**

(D. Tex. Jan. 4, 2010)

#### ***Negligence Claim Sufficient To Trigger Duty to Defend***

Bowen, Miclette & Britt (BMB), and an employee were sued in three separate lawsuits by victims of the Stanford Financial Ponzi scheme. The underlying plaintiffs claimed that BMB rendered professional services to Stanford as insurance agents, brokers, risk managers, and/or insurance consultants. More specifically, the plaintiffs alleged that BMB stated in letters that Stanford was insured by various Lloyd's insurance policies and incorrectly stated that Stanford qualified for such coverage by passing stringent risk management reviews. The underlying plaintiffs contended that these letters implied that the insurance coverage provided safety for all deposits and investments in Stanford.

The plaintiffs sought damages for losses to various CD accounts deposited with Stanford. As a result of the lawsuits, BMB sought coverage under a professional liability policy issued by Endurance. Endurance denied coverage concluding that the claims did not constitute wrongful acts as defined by the policy. In considering the claims asserted against BMB, the court concluded that the claims were based on services that fell within the definition of professional services for the purposes of coverage under the policy.

Endurance also denied coverage based upon an exclusion precluding coverage for losses arising out of violation of federal or state securities laws. The court noted that while the complaint asserted specific claims that BMB violated securities laws, the complaints also included claims for common law negligence. Accordingly, the court concluded that the duty to defend was triggered citing well established case law standing for the proposition that when one claim is covered, the insurer is required to provide a defense against all claims.

***Impact:*** It is apparent there will be no shortage of litigation resulting from the Stanford Ponzi scheme. Arguably, this litigation is creative in that the victims of the Ponzi scheme are seeking recovery from insurance brokers, as opposed to simply the bank itself. That said, clearly the plaintiffs have filed a very broadly worded complaint, and it was sufficient to trigger the duty to defend. As always, it remains difficult for an insurer to escape a duty to defend, even where the majority of the complaint asserts claims that are not covered.

For a copy of this decision, click here: <http://tinyurl.com/GS-PLM-Jan-15>

## QUANTA LINES INS CO. v. INVESTORS CAPITAL CORP.

(S.D.N.Y. Dec. 17, 2009)

### *Despite Withdrawal, Plaintiff's Allegations Constitute A "Claim"*

ICC is a securities broker/dealer. Prior to December 31, 2004, ICC was insured under a professional liability policy issued by Firemen's Fund Insurance Company. From December 31, 2004 to December 31, 2005, ICC was insured under a Broker/Dealer and Registered Representative Professional Liability policy issued by Quanta. (The policy was renewed for the period of December 31, 2005 to December 31, 2006.)

On October 21, 2004, ICC received a letter from an attorney representing an investor, Patricia Alston, claiming that Alston had invested over \$100,000 and as a result of the actions of ICC's representative, Joseph Jones, had sold her unregistered securities (BAB Productions). After a brief investigation, it was determined that Jones had, in fact, invested in a different securities fund. After a conversation with claimant's counsel, it was agreed that the letter could be disregarded and that no claim was being pursued against ICC by Alston. This letter and the investigation were subsequently reported to Quanta a year and a half later on May 8, 2006.

Beginning on August 12, 2005, ICC was served with a series of arbitration demands relating to the selling of the BAB security by Jones. In response, ICC sought coverage under the Quanta policy. Quanta denied coverage concluding that the Alston letter and the underlying arbitrations were part of a single claim that arose out of an interrelated wrongful act that occurred prior to the inception date of the policy.

The initial question addressed by the court was whether the Alston letter constituted a claim as defined by the policy. Accordingly, the court held that the term "claim" was not ambiguous and the Alston letter alleged a specific wrongful act as contemplated by the policy. The court noted that the allegation clearly included a claim of negligent supervision and *respondeat superior* liability against ICC which qualified as a negligent act or omission committed by an insured.

Finally, the court held that there was a sufficient factual nexus between the Alston letter and the underlying arbitrations, i.e. Jones' sale of unregistered BAB securities and ICC's failure to supervise such sales. The court stated that even though ICC's investigation determined that Ms. Alston did not actually invest in BAB, the veracity of the allegations, or lack thereof, did not erase the fact that the allegations were made and were consistent with the factual allegations in the underlying arbitrations. Accordingly, ICC was not entitled to coverage.

**Impact:** This case is interesting because the Alston letter was deemed a claim despite the fact that it contained factual inaccuracies and was later withdrawn. This court applied a very mechanical interpretation of the policy and arguably stretched the limits of the definition of the term claim to find an interrelated act. It will be interesting to see whether this case gets appealed to the Second Circuit and what resulting decision the court will reach.

For a copy of this decision, click here: <http://tinyurl.com/GS-PLM-Jan-15>

## **SCOTTSDALE INS. CO. v. ATTORNEYS PROCESS & INVESTIGATION SERVICES, INC.**

(Ct. of App., Iowa, Dec. 17, 2009)

### ***Potential Negligence Claim Triggers Duty to Defend***

The Sac & Fox tribe operated a bingo casino hotel in Iowa. A dispute arose between two factions of the tribe, the Elected Tribal Council and the Appointed Tribal Council. On March 26, 2003, the Appointed Tribal Council seized control of the casino. Notably, at the time, the Elected Tribal Council was recognized by the United States as the leadership body of the tribe. On June 16, 2003, APIS entered into a written agreement with a member of the Elected Tribal Council for the purposes of investigation, security, and law enforcement consulting services. On October 1, 2003, employees of APIS entered the tribe's community center and casino and remained on the premises for less than 24 hours.

The Appointed Tribal Council was later lawfully elected and recognized by the federal government as the governing council. The tribe subsequently filed a tort action against APIS alleging unauthorized possession of monies in excess of \$1 million, intentional trespass, intentional destruction of property, unlawful arrest, battery, and false imprisonment. APIS sought coverage under a commercial general liability policy which included personal advertising injury coverage, as well as errors and omissions coverage.

With respect to the errors and omissions coverage, APIS argued that even though the complaint asserted intentional causes of action, a fact finder addressing the merits of the complaint could find APIS negligently or mistakenly entered the tribe's property. APIS noted that it believed it had authority from a member of the Elected Tribal Council to engage in the acts that were the subject of the complaint.

While the court noted that there would be no duty to indemnify damages awarded for criminal conduct or damages based upon conversion, the court agreed that the duty to defend was triggered. The court held that if a claim rationally falls within the insurance coverage, an insurer is required to defend the entire action.

***Impact:*** This case is interesting in the fact that the complaint appears to have only alleged intentional actions. Despite this, the court held that there was a reasonable possibility that a fact finder could determine negligence. It is well established that the duty to defend is extremely broad, and it remains very difficult for an insurer to escape this obligation.

For a copy of this decision, click here: <http://tinyurl.com/GS-PLM-Jan-15>

**PANAGORA ASSET MANAGEMENT, INC. v. ST. PAUL MERCURY INS.**  
(D. Mass. Dec. 14, 2009)

***Reimbursing Client's Loss Is Not Mitigation As Defined By Policy***

PanAgora received instructions from its client, Shell Oil, to construct three portfolios for execution. In light of a short deadline, PanAgora went outside its normal procedures and used an Excel spreadsheet to construct the portfolios. As a result, PanAgora over weighted the portfolios, resulting in a loss of approximately \$2 million.

On December 4, 2008, PanAgora notified Travelers of the loss. On December 16, 2008, PanAgora wrote Travelers to inform them of the loss inquiring whether any claim by Shell would be covered under the policy. On January 9, 2009, Travelers denied coverage for the loss, and PanAgora subsequently settled the claim by crediting the sales portfolios in excess of \$2 million on March 3 and March 5, 2009. PanAgora then sought coverage under an errors and omissions policy issued by Travelers.

The policy provided coverage in the amount of \$5 million with a \$500,000 retention. The policy also had an endorsement which provided that the insurer would reimburse the policyholder for costs incurred by the policyholder to mitigate or correct direct monetary damages to a customer. Coverage would exist under the endorsement to the extent a claim would result in the absence of such mitigation. This endorsement contained a \$2.5 million retention.

Travelers argued that the payment to Shell Oil fell within the scope of the endorsement, thereby triggering the \$2.5 million retention.

The court disagreed. The court stated that according to the plain meaning of the endorsement, it applied where the policyholder covers a client's loss prior to any claim being made for the sake of an ongoing client relationship. The court stated that the usual and ordinary meaning of the word reimburse implies the incurrence of a cost by the policyholder in correcting a mistake which must be repaid to the policyholder by the insurer. Prior to the settlement, no monies were paid to Shell as a result of PanAgora's actions. Therefore, the court concluded that without payment to Shell by PanAgora, Travelers was not, either at the time of the letter or any time prior to the claim by Shell, in a position to reimburse any costs incurred in repaying the loss. Accordingly, the court concluded that the endorsement was never invoked by PanAgora.

***Impact:*** The court's resolution of this case seems to turn on timing, more than anything else. Here, the court stated that at the time of the letter providing notice to Travelers, there was no payment to Shell and, therefore, there was nothing to reimburse. Accordingly, the endorsement did not apply. That said, it is uncertain why the endorsement would not apply after the policyholder made the payment and then sought reimbursement. This remains a confounding decision.

For a copy of this decision, click here: <http://tinyurl.com/GS-PLM-Jan-15>

## **CONTINENTAL CAS. CO. v. AUTO PLUS INS. AGENCY, LLC**

(N.D. Ohio, Dec. 11, 2009)

### ***Automatic Renewal of Underlying Policy After Retroactive Date Does Not Trigger Coverage***

This case involves a number of parties seeking coverage. The entire dispute originated from a property damage claim caused by a fire. The owner of the damaged property had obtained an insurance policy from Auto Plus (through his agent, Billings). However, the casualty policy obtained by Auto Plus failed to cover all of the damage caused by a fire. As a result, the policyholder filed suit against Auto Plus and Billings. In response, the professional liability insurer for Auto Plus and Billings, Continental, filed a declaratory judgment action seeking a declaration of rights under the policy.

As a result of the denial, Auto Plus and Billings filed a lawsuit against their own broker who obtained professional liability coverage for Auto Plus. This second action alleged that Professional Insurance Agents Association and Calsurance were negligent in failing to obtain adequate coverage for claims made under past policies. All parties filed motions for summary judgment.

### ***Continental Casualty v. Billings and Auto Plus***

Continental sought a declaration that it owed no duty to provide coverage to Auto Plus and Billings because the loss occurred before the retroactive date included in the policy. Continental argued that the wrongful act at issue was Auto Plus' failure to provide sufficient coverage for the underlying loss when the underlying policy was initially placed in 2002. Accordingly, the wrongful act occurred prior to Continental's retroactive date (2004). Auto Plus argued that because the underlying lawsuit alleged that there was a breach of duty each year the policy was renewed and the renewals occurred at the retroactive date, the policy was triggered. The court noted that Auto Plus' argument "on the surface" suggested the complaint stated a claim that was covered by the policy. However, the court also noted that it was undisputed that Auto Plus and Billings had no involvement in the yearly renewals of the policy.

Accordingly, despite the fact that yearly renewals occurred after the Continental policy came into effect, the wrongful act occurred prior to the retroactive date. Therefore, Continental was not required to provide coverage.

### ***Billings v. Calsurance***

As noted, Billings filed suit against Calsurance and PIA as a result of Continental's denial. Billings argued that he relied on Calsurance to advise him of the effect of the E&O policy and to make sure that he would continue to be provided coverage. The court noted that under Ohio law, an agency has no specific duty to advise a client unless the agency knows that the customer is relying upon its expertise. Here, Billings did not allege that Calsurance provided insufficient coverage, but rather, claimed that Calsurance failed to educate him about the consequences of terminating a prior policy. However, because the complaint failed to assert that Billings was relying on Calsurance's expertise Billings could not assert a valid claim.

### ***Billings and Auto Plus v. PIA***

Billings and Auto Plus claimed that PIA failed to obtain adequate insurance coverage and failed to inform Billings of potential future liability for claims made under past insurance policies. In short, the court concluded that summary judgment in favor of PIA was appropriate, because Billings had not offered the slightest bit of evidence that PIA breached any duties owed to Billings.

**Impact:** At a minimum, this case illustrates how a single property loss can generate multiple layers of professional liability claims. Here, an insurance agent was caught in a situation where he did not have coverage for an underlying claim. It is important to note, especially in the context of insurance broker litigation, the elements each jurisdiction requires for a valid claim to exist. Here, under Ohio law, it is essential that a client plead and prove that the agency knew the customer was relying upon its expertise in order to fashion a valid cause of action. It was Billings' failure to present such evidence that doomed his claim.

For a copy of this decision, click here: <http://tinyurl.com/GS-PLM-Jan-15>

### **III. Professional Malpractice**

#### **SMITH v. OHIO BAR LIABILITY INS. CO.**

(Ct. App. Ohio, Dec. 16, 2009)

#### ***Sale of Annuities Triggers “Business Enterprise” Exclusion***

Anthony Smith operated as a lawyer in the law firm of Karl & Smith, LLC, while also owning and operating the Anthony J. Smith Agency, Inc. The agency provided services which included the sale of annuities. Lester and Thelma Otto purchased annuities from the Agency. In addition, Anthony Smith also performed some estate work for the Ottos, some of which was funded by the annuities. Subsequent to the purchase, the Ottos filed suit against Anthony Smith, the Agency, as well as Karl & Smith, LLC.

After suit was filed, Anthony Smith sought coverage under a professional liability policy issued by the defendant (OBLIC). The policy named Karl & Smith, LLC, Anthony Smith, and Margaret Karl as insureds. OBLIC undertook the defense under a reservation of rights. OBLIC reserved its right to deny coverage based upon the application of the “business pursuits” exclusion. Plaintiffs filed a declaratory judgment seeking a declaration of rights under the policy. This exclusion excluded coverage for losses arising out of a business enterprise not named in the Declarations.

The court noted that the deposition testimony indicated that the Ottos did not sue Anthony Smith based upon dissatisfaction with his legal work, but rather, in relation to the sale of the annuities. Apparently the Otto's concern was the way the annuities were structured, i.e., they did not have any control over them. While Smith did indeed perform some legal work, the court concluded that the legal work had its origin in the investments themselves. Accordingly, the court concluded under the facts of the case, the Ottos claims would not fall under the definition of “professional services” to invoke coverage in the first place, notwithstanding the potential application of the exclusion.

**Impact:** This case is another example where coverage for the claim is simply outside the scope of the policy. The policy specifically identified which parties were insured - the law firm. Here, the agency performed the work that gave rise to the claim and, therefore, there was no coverage under the policy.

For a copy of this decision, click here: <http://tinyurl.com/GS-PLM-Jan-15>

**NARDELLA CHONG, P.A. v. MEDMARC CAS. INS. CO.**  
(N.D. Fla. Dec. 10, 2009)

***Restitution Payments Do Not Trigger Coverage Under a Professional Liability Policy.***

Plaintiff was a professional association of attorneys insured under a lawyer's professional liability policy. In April 2007, the plaintiff was contacted via e-mail by Mr. Liu Chang who represented himself to be president of Northlink Industrial, Ltd. At Mr. Chang's request, plaintiff accepted the representation of Northlink as a client of the firm. In the same month, the plaintiff received a cashier's check purportedly to be on behalf of Northlink in the amount of \$197,000. The plaintiff deposited the check into the firm's trust account, where it was held with trust funds belonging to other clients.

The plaintiff subsequently received instructions from Mr. Chang to make wire transfers of portions of the check. Plaintiff complied. Since the cashier's check had not yet cleared at the time of the wire transfer, other client's funds were utilized to fund the wire transfer. The check was later determined to be counterfeit. Plaintiff replenished the trust accounts with its own money.

Subsequently, plaintiff sought coverage under the professional liability policy. Defendant insurer denied coverage contending that the payment of funds was essentially restitution and/or recoupment of money paid to cover the monies wrongly transferred as part of the fraud committed by Mr. Chang. The court agreed, stating that the plaintiff's claims are properly characterized as restitutionary and would not constitute damages under the policy. The loss was not the result of negligence on the part of the firm, but rather a fraud perpetrated by Northlink. Accordingly, coverage was properly denied.

**Impact:** As an initial point, this case serves as a reminder as to what can happen when one actually believes random e-mails from unknown senders promising fortunes in response to legal assistance in the States. Here, the court correctly characterized the issue as one of restitution as opposed to negligence. The law firm at issue was the victim of fraud, not the perpetrator of malpractice. Accordingly, the loss was properly excluded as outside the scope of the policy.

For a copy of this decision, click here: <http://tinyurl.com/GS-PLM-Jan-15>

## IV. Medical Malpractice

### **ISMIE MUT. INS. CO. v. MICHAELIS JACKSON & ASSOC., LLC**

(App. Ct. Ill. Dec. 30, 2009)

#### ***Qui Tam<sup>1</sup> Suit Does Not Constitute Claim For Personal Injury***

Former employees of Jackson & Associates filed a *qui tam* suit alleging that Jackson had performed numerous medically unnecessary cataract surgeries and invasive follow-up procedures. The complaint asserted that the number of unnecessary procedures measured in the thousands and thereby defrauded Medicare of tens of thousands of dollars. During the years, these purportedly unnecessary procedures were done, Jackson was insured under a medical malpractice policy issued by the plaintiff.

In response to the claim, the plaintiff insurer undertook the defense of Jackson pursuant to its supplementary payment section which provided \$30,000 in coverage for claims related to Medicare investigations. Once this coverage was exhausted, plaintiff notified Jackson that no further payments would be made and filed the instant declaratory judgment.

Plaintiff contended that the *qui tam* action did not involve a claim for personal injury and therefore, the action was outside the scope of the remaining coverage provided for in the policy. Jackson argued that in keeping with the plain language used in the contract, coverage existed if the claim is for damages that involved personal injury. The court soundly rejected this contention and stated that the allegation at issue in a *qui tam* case was false billings which have nothing to do with alleged bodily injuries to patients.

The court went on to note that while the insurer might have to defend a medical malpractice claim stemming from the purported unnecessary procedures, this does not require a finding that the same insurer is required to defend a *qui tam* case tied to the same allegations.

**Impact:** In this case, the dispute came down to whether the claim was within the contemplation of the policy. The policy did provide limited coverage in the context of Medicare investigation; however, the *qui tam* action was clearly outside the scope of the professional liability policy. To hold otherwise would have made the plaintiff the insurer of the policyholder's compliance with Medicare standards. Such is clearly not the intent of a professional liability policy.

For a copy of this decision, click here: <http://tinyurl.com/GS-PLM-Jan-15>

## V. News and Notes

### ***The Professional Liability Defense Federation Unveiled In September 2009***

September 2009 saw the launch of the Professional Liability Defense Federation. This organization is devoted to the defense of claims against attorneys, health care professionals, accountants and

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<sup>1</sup> *Qui tam* suit is an action brought by an informer under a statute which establishes a penalty for the commission or omission of a certain act. Black's Law Dictionary, Sixth Edition.

architects and is committed to providing state-of-the-art insights to members and the broader defense community of claims management and law developments important to this field. If you would like more information about the PLDF, visit [www.pldf.org](http://www.pldf.org) or email Albert J. D'Aquino at [ajdaquino@goldbergsegalla.com](mailto:ajdaquino@goldbergsegalla.com)

### ***U.S. Senator Calls for Investigation Into E-Mails Sent To AIG***

Sen. Bunning of Kentucky, alarmed by a purported email exchange where representatives of the New York Fed advised AIG to withhold information from the SEC, has called for an investigation. It has been reported that the e-mails placed pressure on AIG to limit disclosure about payments to Goldman Sachs Group Inc., Societe Generale AG and other global banking firms.

For a full copy of this article, click here: <http://tinyurl.com/GS-PLM-Jan-1>

### ***Concerns Over New York Fed and AIG Results in Subpoenas***

Not surprisingly, a House government oversight panel ordered the Federal Reserve Bank to disclose documents concerning its role in AIG's failure to disclose details concerning payouts to trading partners.

For a complete copy of this article, click here: <http://tinyurl.com/GS-PLM-Jan-6>

### ***Insurers Investment Income Continues to Suffer***

Dr. Robert Hartwig, president and economist at the Insurance Information Institute, has reported a 50% decrease in insurers' investment income for 2008, with the drop continuing in 2009. He blames, in part, the Fed's commitment to maintaining low interest rates.

For a full copy of this article, click here: <http://tinyurl.com/GS-PLM-Jan-2>

### ***Health Insurers Lobby For Changes to Healthcare Bill***

Health insurers are hoping for changes to pending health legislation seeking to eliminate caps on profits and other administrative spending. The proposed bills set limits as to the amounts insurers can dedicate to medical care versus administrative costs, profits and other areas, an allocation that has been termed medical-loss ratios. Insurers fear that the legislation will cap profits and significantly alter how companies operate.

For a complete copy of this article, click here: <http://tinyurl.com/GS-PLM-Jan-3>

### ***Chinese Drywall Trust Files Suit Against 14 Insurers***

WCI Drywall Trust was formed after WCI Communities filed bankruptcy. Currently, over 700 homeowners can seek recovery from the Trust for losses arising out of homes constructed with Chinese drywall. WCI is seeking a declaration of coverage under a series of policies providing coverage in the amount of \$200 Million.

For a complete copy of this article, click here: <http://tinyurl.com/GS-PLM-Jan-4>

### ***New York May Move Forward With Insurance Exchange***

As part of Governor Paterson's State of the State address, he announced an initiative to reconstitute the New York Insurance Exchange. The Exchange would be akin to the Lloyd's of London style marketplace.

For a complete copy of this article, click here: <http://tinyurl.com/GS-PLM-Jan-5>

### ***Most of Damage Caused By Haiti Earthquake Is Likely Not Insured***

Risk Management Solutions of Newark, Calif., citing information from London-based AXCO, states that Haiti remains one of the smallest markets in the Americas with a total non-life premium income of \$20 Million. Early estimates place the costs of the economic damages in the hundreds of millions of dollars.

For a copy of this article, click here: <http://tinyurl.com/GS-PLM-Jan-7>

### ***Travelers Successfully Litigates Coverage Under Employment Practices Policy***

Travelers declined to provide coverage to a policyholder for losses arising out of a wrongful discharge action. Travelers relied on an exclusion precluding coverage for "administrative or regulatory" proceedings. The court agreed with Travelers, concluding that the unemployment benefit proceeding was clearly an administrative proceeding as contemplated by the policy.

For a copy of this order, click here: <http://tinyurl.com/GS-PLM-Jan-15>

### ***Court Enters Stay While National Union Seeks Appeal***

The policyholder has filed a motion for summary judgment seeking the advancement of defense costs resulting from a criminal action against certain directors and officers. National Union had filed a motion for summary judgment seeking a declaration that the prior acts exclusion would bar the advancement of defense costs. The court denied the insurer's motion. However, a stay was entered allowing for an appellate court to review this denial.

For a copy of the order, click here: <http://tinyurl.com/GS-PLM-Jan-15>

### ***Agent Brings In Two Brokers In Litigation With Lloyd's***

Liberty Syndicates at Lloyd's filed suit against Walnut Advisory Corp seeking damages in excess of \$6 Million for purported violations of a binding authority agreement. Walnut filed the third-party complaint in an effort to pass liability onto Carman Corp. (local retail broker) and Miller Insurance Services (designated Lloyd's broker).

For a copy of the complaint, click here: <http://tinyurl.com/GS-PLM-Jan-15>

### ***Film Company Files Suit Against Broker Alleging Defective Policy***

Capital Films has filed suit against an insurance broker contending the policy at issue did not provide the proper coverage. More specifically, it did not cover for losses that resulted when Samuel L. Jackson sustained a back injury and could not complete the film. The complaint seeks damages in the amount of \$20 Million.

For a copy of the complaint, click here: <http://tinyurl.com/GS-PLM-Jan-15>

### ***Entergy Files Suit Against Army Corp For Katrina Losses***

Entergy and its insurer, Hartford Steam Boiler Inspection and Insurance Company, have filed suit against the Army Corps of Engineers alleging that the negligent construction of levees and canals caused the widespread damage resulting when Hurricane Katrina came ashore.

For a copy of the complaint, click here: <http://tinyurl.com/GS-PLM-Jan-15>

### ***Insurer Files Suit Claiming Fraudulent Billing Practices***

This dispute originated when a Florida law firm brought suit against Lexington alleging Lexington wrongfully terminated a standing business relationship. In response, Lexington filed a countersuit alleging the law firm over billed Lexington in the millions.

For a copy of the complaint, click here: <http://tinyurl.com/GS-PLM-Jan-15>

## **VI. The Insurance Agents' and Brokers' E&O Report**

### **How Insurance Agencies and Brokerages Can Benefit From the Upside of Social Networking While Minimizing the Downside of a Possible E&O Risk**

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Colleen and Rick have known each other since they were 12 years old, when "social networking" consisted of hanging out at the mall or calling someone on the phone – two things that, even for 12 year olds, have become passé, giving way to Facebook, instant messaging, and shopping on-line.

As an insurance agent and broker E&O attorney since 1992, one exciting challenge has been to keep up with the changing ways insurance agents and brokers do business. There have been numerous changes over the years, many driven by new technologies. Do you remember "T- filing" or when voice mail and faxing were considered "high tech?" The reason for keeping up with these many changes is to enable us to better predict new or increased E&O exposures associated with new business methods and then determine how to minimize them. The trick has always been to separate a true E&O risk generated by new technologies from those which turn out to be just speculative. Recall the "chicken little/the sky is falling" mentality surrounding Y2K?

Most insurance agencies and brokerages, including those that are exclusively paper filing or routinely taking insurance orders on cocktail napkins, have noticed that social media networking is rapidly expanding the ways in which insurance agencies and brokerages do business. The question no longer appears to be "whether" an agency or brokerage will become involved in social media networking but "when" and "to what extent." This merits an examination of the E&O risks which may flow from this emerging way of transacting insurance business.

In preparing to share this article with you, we first had a virtual interview with Jeff Cobb, to learn some of the basics an agency or brokerage faces when deciding to become involved in social networking. Jeff Cobb is an Internet marketing and social media specialist who teaches organizations, including insurance agencies and brokerages, to leverage the social Web for maximum impact.

We then spent some time reading what others had written about the potential resultant E&O exposures of social media networking. We analyzed this information in light of our experience defending hundreds of insurance agents and brokers over the years and thought about what an agency or brokerage could do to begin minimizing the "downside" of social media networking.

Below we share both our interview with Jeff Cobb as well as what we think can help you neutralize the major potential E&O exposures. Since it is not meant to be an exhaustive list, but rather a starting point, we provide some links for those of you who want to delve further into this topic. In addition, we welcome any questions or comments you may have via e-mail to [cmurphy@goldbergsegalla.com](mailto:cmurphy@goldbergsegalla.com), [rcohen@goldbergsegalla.com](mailto:rcohen@goldbergsegalla.com), or [cbelter@goldbergsegalla.com](mailto:cbelter@goldbergsegalla.com).

## A Virtual Interview with Jeff Cobbs

### 1. What is social media networking?

“Social media networking is fundamentally just a conversation. What makes it so different is that the Web now makes it possible for that conversation to happen worldwide, 24/7, and involves pretty much anyone who wants to participate. I tell people to write down the name of a place where they have traditionally gone to network - maybe a Chamber of Commerce event, or a Rotary Club - and then write ‘times infinity’ after it. That’s the potential of ‘social networking.’”

### 2. Why would insurance agents and brokers want to be involved in this?

“Because their customers and prospects are already in that conversation. So are their competitors. And in most cases, the conversation drives buying decisions much more effectively than traditional media-like advertising and direct mail.”

### 3. What are three things agents and brokers can do to get started?

“Listen. Experiment. Focus. Don’t just jump in - start with listening. Use tools like Google Alerts, (<http://www.google.com/alerts>), Google blog search (<http://blogsearch.google.com>), and Twitter search (<http://search.twitter.com>) to find people who are saying interesting things related to your field, and start following those people. See how they do it, and then start trying out a variety of the tools, just to get a feel for them. Set up a Twitter account, a LinkedIn account, or a Facebook account for yourself if you haven’t already. Try doing a few blog posts on a popular free service like Wordpress.com (<http://wordpress.com>). Get a feel for what seems to work for your organization and your customer base, and then focus in on one initially and do it really well. Don’t scatter yourself all over the place or you will be overwhelmed with the effort of keeping up.”

### 4. What would social media networking look like in an insurance agency or brokerage using it at a high level?

“I think the two biggest opportunities for an agency are to learn to listen really well on the Web and then to use what it hears to provide targeted expertise and guidance to its audience. Use key listening tools like Google Alerts and Twitter Search to find out what people are saying about key topics where you can add value. Then use tools like a blog or Twitter to offer expert advice or point people to valuable resources on the Web. This approach attracts attention to your agency without hard selling, and over time it establishes you as the trusted, go-to source when prospects and customers make buying decisions about insurance.”

**5. Why would insurance agents and brokers want to consider possibly having someone help them do this?**

“Taking some basic steps like setting up Google Alerts and monitoring them, or starting a blog, is not really all that hard. In fact, I recommend that agencies take a stab at some simple steps on their own as a way to start moving up the learning curve. But when it comes to really being engaged in the social Web and getting maximum return on investment, there are a lot of moving parts. Very few agencies have the internal know-how and resources for creating and executing on a full-blown social media marketing strategy. Bringing in outside expertise can really help jump-start the effort and also ensure that it stays on track over the long haul.”

- *For a PDF of Jeff Cobb’s Making Social Media Networking Work for Your Agency, go to <http://www.jeffthomascobb.com/social-media-for-agencies>*
- *For a detailed review of a recently published article regarding how to use social media written by Daniel Gerber, Esq., Chairperson of Goldberg Segalla’s Global Insurance Services Group and Michael D. Shalhoub, Esq., a partner at Goldberg Segalla, entitled, “To Tweet or not to Tweet, Understanding the Synergy Among Social Media”, go to: <http://tinyurl.com/Gerber-Art>*
- *For the Agents Council for Technology’s resource designed to assist agents to develop a social web policy, go to: <http://is.gd/5MsJJ>*

**Minimizing the E&O Exposure of Social Media Networking**

Now that your agency or brokerage has or is considering getting involved in social media networking, it’s time to think about how you can best do this while ensuring that you will not find yourself in a social media networking E&O claim or lawsuit. You will notice that although we are dealing with cutting-edge exposures, the corresponding E&O tips remain the tried and true methods of implementing and following agency-wide written practices and procedures, and documenting your file that you have done so. What follows is what we believe to be the major E&O exposures associated with social media networking, along with suggested E&O loss control tips to minimize your exposure.

We offer these tips to you with the following caveat - just as it is a business decision whether your agency gets involved with social media networking, it is also a business decision whether you implement any suggested E&O loss control techniques. One item we strongly suggest you do implement is to consider increasing your E&O limits to keep pace with the expanded ways in which you are doing business.

## **Business Defamation/Trade Libel**

Business defamation and trade libel are business torts that have been around for as long as businesses have been competitive with each other. With the dawn of the Internet and, more recently, social networking sites, these torts (sometimes referred to as “cyber slander” or “internet disparagement”) have become of more concern for many businesses that have employees utilizing Twitter, Facebook, LinkedIn and company sponsored blogs for business and personal uses. Simply stated, business defamation is a false statement about a business, its products or services that interfere with the company’s business relations through damaging or derogatory remarks about its products or services that cause customers of those products and services to look elsewhere.

Over the years as E&O attorneys, we have occasionally been called upon to defend insurance agencies and brokerages in such claims. Due to the nature of social media networking, there is a potential for increased exposure to agencies and brokerages for business defamation claims if they are not mindful. Why? Because information you or your employees post on social networking sites is transmitted instantly and can be redistributed to other sites worldwide without your knowledge. Once posted, your information can remain on the “social web” forever. In addition, social networking sites encourage more casual discussions that in the pre-Internet days may have been confined to the office water cooler. Obviously these casual conversations are not suited to the business discussions surrounding insurance transactions and should not be published on the Internet.

Casual conversations seem to be the new standard for doing business especially on social networking media sites. Twitter, for example, promotes a “direct feed” into a user’s mind, by asking the question “what are you doing now?” Yet a direct feed into some insurance agents’ or brokers’ minds may be enough to cause an E&O attorney to wake up in a cold sweat in the middle of the night.

These casual conversations also move very quickly on social networking sites and often use abbreviations, nicknames and slang which make it more difficult to be clear or precise resulting in misinterpretations and miscommunications. In addition, in an effort to distinguish and promote the insurance agency or brokerage, employees can intentionally, carelessly or unwittingly make a comment about a competitor insurance agency or insurer which the competitor finds insulting or harmful to its business reputation or disparaging of its services or products. Lastly, discussions can become heated and an insult hurled before the tweeter/blogger counts to the proverbial 10. The fast-paced casual nature of the conversation can result in posts which end up as the basis for a trade libel or a business defamation lawsuit against the insurance agency or brokerage.

One of the best ways to avoid a business defamation claim is to understand what it is. To help you with this, we provide the following basic introduction to the law of defamation. We do so for educational purposes only. Insurance agencies and brokerages are urged to personally consult with a defamation attorney to assist the agency in writing a policy regarding the use and risks associated with social media networking.

The legal definition of defamation varies state by state. In New York, for example, to constitute defamation, plaintiffs must prove that the defendant made a false statement, published that statement to a third party without privilege, with fault measured by at least a negligence standard, and that the statement caused special damages or constituted “defamation per se.” A false statement constitutes “defamation per se” when it charges another with a serious crime or tends to injure another in his or her trade, business, or profession. *Geraci v. Probst*, 2009 N.Y. Slip Op 2971, 2 (N.Y. App. Div. 2d Dep’t 2009) (emphasis provided).

Defamation has long been recognized in New York State to arise from “the making of a false statement which tends to ‘expose the plaintiff to public contempt, ridicule, aversion or disgrace, or induce an evil opinion of him in the minds of right-thinking persons, and to deprive him of their friendly intercourse in society.’” (*Foster v Churchill*, 87 NY2d 744, 751).

In evaluating whether a cause of action for defamation is successfully pleaded, the words must be construed in the context of the entire statement or publication as a whole, tested against the understanding of the average reader, and if not reasonably susceptible of a defamatory meaning, they are not actionable and cannot be made so by a strained or artificial construction. “[C]ourts ‘will not strain to find defamation where none exists.’” (*Cohn v National Broadcasting Co.*, 50 NY2d 885, 887, cert denied 449 US 1022).

Truth provides a complete defense to defamation claims. A cautionary note is in order here; by the time a defendant has proven the truth of an alleged defamatory statement, time and resources have been wasted.

Thus, agencies and brokerages should have a policy in place that mandates that their employees refrain from making statements on the social web that your competitors might find unflattering or disparaging. The arguable truth of the statement or comment should not dictate whether the comment should be published on the Internet. Disparaging comments lead to litigation and anything that creates the potential for such claims should be avoided.

Sabrina Sally, CPCU of The E&O insurer, Swiss Re, has recently issued the following advice about whether an insurance agent or broker’s blog post may be viewed as commercial speech entitled to only limited First Amendment protection: “Keeping in mind that commercial speech – speech which proposes an economic transaction – is entitled only to limited First Amendment constitutional protection, there is a real question as to the level of First Amendment protection business representatives will receive when they write or respond to a blog. The answer is not yet clear.” As this area continues to develop, you would be well served to consult with legal counsel experienced in First Amendment law for guidance on creating the agency’s policy regarding the content you will permit on blogs on your agency’s behalf. For more from Sabrina Sally, CPCU, see her article entitled *Agency E&O Considerations When Using Social Media*:

[http://www.iiaba.net/na/16\\_AgentsCouncilForTechnology/NA20090715142908?ContentPreference=NA&ActiveState=AZ&ContentLevel1=ACT&ContentLevel2=&ContentLevel3=&ActiveTab=NA&StartRow=0](http://www.iiaba.net/na/16_AgentsCouncilForTechnology/NA20090715142908?ContentPreference=NA&ActiveState=AZ&ContentLevel1=ACT&ContentLevel2=&ContentLevel3=&ActiveTab=NA&StartRow=0)

Many of you may choose to blog by posting insurance industry articles and/or providing a topical news feed to your targeted customers. You may wish to consider your potential exposure for republishing an article which is then claimed to contain defamatory information. Section 230 of the Communications Decency Act provides some protection from liability to “information service providers” such as websites or blogs related to the publication of information from third parties. However, if the service provider creates or develops, in whole or in part, the subject information they will be deemed to be content providers and not protected by Section 230. Thus, for example, publishing information received from a third party but adding your own commentary or additional material can move your website or blog from being an information provider to a content provider.

Many of you may be aware that the defamation suits arising out of social media networking have already been filed. In one of the first such suits, a [Chicago apartment management company sued a former tenant for defamation via Twitter](#). Horizon Group Management LLC filed a lawsuit in the Circuit Court of Cook County on Tuesday (28th of July ‘09) claiming Amanda Bonnen of Chicago defamed the company in a May message on Twitter. It is alleged that Amanda Bonnen tweeted the comment: *“You should just come anyway. Who said sleeping in a moldy apartment was bad for you? Horizon Realty thinks it’s okay.”* The apartment management company has sued claiming that the casual comment made by one of its former tenants is false and has damaged its business reputation. This is a good example of the type of casual comment which may arguably prove to be actionable. With that in mind, let’s turn to the related E&O loss control prevention tips.

There are many good reasons to have a written social media networking policy for your business and employees. The reasons for a written policy extend beyond just protection from business defamation claims. This type of policy can protect against employment discrimination claims, false or misleading advertising claims and the inadvertent disclosure of proprietary business information. As with any written policy of this type, you should consult with an attorney that is experienced in this area of practice to draft or review your policy before it is implemented.

Here are a few items to consider with respect to any written social media networking policy:

- A written social media networking policy may provide your business with a very strong defense to business defamation lawsuits. The policy should forbid employees from making comments about business competitors or their products, services or employees. Without a written policy, how will your business establish that your employee was acting outside of the scope of his employment or against its policies when he posted false statements about a competitor or its services on a social networking site?
- A written social media networking policy should be designed to protect against employees making inappropriate comments about co-employees and supervisors.

- A written social media networking policy should be designed to guard against your employees making false or unsupported claims about your own products or services that may be mistakenly relied upon by potential customers. These types of comments can lead not only to disgruntled customers, but suits based on false and misleading advertising or even consumer fraud.
- A written social media networking policy should make it clear that confidential or proprietary information about the company is not to be disseminated or discussed in social networking sites or blogs.
- It should be made clear in a written social media networking policy that social networking sites related to a company's business should never be used for personal business or inappropriate reasons.
- Insurance agency and brokerage staff should be trained regarding the social media networking policy.

For more information concerning this topic see *Creating a Social Web Policy For Your Independent Agencies*, An Agents Council for Technology Report, at <http://is.gd/5MsJJ>.

A comprehensive agency-wide, regularly followed, written anti-defamation policy should be developed with the advice of your counsel and at a minimum ought to do the following:

- Advise the agency and brokerage staff that there is absolutely no such thing as an “off the record” conversation and that they should guard against making hasty remarks while on the social web which may be construed as defamatory in nature.
- The foregoing advice obviously includes absolutely no derogatory remarks (true or not) about the insurers, insureds, or competitor insurance agencies and brokerages.
- Instruct that a staff member agent or broker must seek permission from agency management before posting about a competitor agency, for example, as a way to promote the agency.
- Have a policy for issuing retractions or corrections with respect to insurance articles and news feeds on the agency's blogs or website.
- Instruct that defamation claims or potential claims are to be brought to the attention of agency management for timely reporting to the involved E&O insurer.

### **The Insurance Agency and Brokerage Must Take Care Not to Post Other's Private Information on the Social Web**

Insurance agencies and brokerages have been required for years now to keep private their customers' confidential information and/or to only use it for certain defined permissible purposes. For example, The Fair Credit Reporting Act and The Driver Privacy Protection Act require agencies to keep information about their clients' insurance scores and personal information on their motor vehicle records confidential.

It is of utmost concern that ALL private information of your customers, employees, etc., be kept off the social web entirely, particularly in light of the devastating potential consequences associated with failing to do so. Private information has been defined as follows: “information which has been provided for specific purposes by an individual and which the individual can reasonably expect will not be made public.” With respect to the social web this would include, but not be limited to, something as basic as the individual’s home address and telephone number, as well as their medical records, insurance score, social security number, etc.

### **Suggested E&O Loss Control Prevention Tips**

- Discuss privacy with your agency staff and implement a written agency policy concerning privacy that encompasses the social web.

### **Failure to Procure Insurance/or to Timely Report a Claim**

While it may represent social networking at its best to post twitter and blog about topics regarding insurance related to your general potential targeted clients, once the discussions turn to insuring specific risks for specific customers, they need to take place off the social networking site, at the earliest opportunity. Agencies and brokerages need to guard against someone on the site later construing a “casual comment” as an agreement to procure, alter or bind coverage resulting in an uncovered claim. While these types of E&O claims may seem rather remote, it makes sense to prevent them by placing disclaimers on your posts about the inability to procure, bind, or alter coverage or report claims, on these sites.

Be aware that an existing client may contact an agent or staff member through, say a LinkedIn email or blog group, and attempt to report a claim or to add coverage to an existing policy. The risk is that since the customer is by-passing normal agency workflow, the transaction might not get processed.

### **Suggested E&O Loss Control Prevention Tips**

- Advise all agency staff that once social networking discussions become specific regarding insuring a particular risk etc., they are to take the discussion off the social networking site and proceed through the normal agency channels. It is also a good idea to keep a copy of any insurance inquiry that was initially received on the social networking site and to include it as part of the client’s file. You should save all e-mails exchanged with an insured or insurer to that particular insured’s file.
- Use a disclaimer stating that the information provided is intended to be related to general situations only and that questions related to specific risks and individuals need to be assessed individually using the agency’s regular workflow for such consultations. ACT Releases Social Media Policy Paper (National Underwriter) <http://is.gd/5MsJJ>.
- Also, consider including the same disclaimers on the agency’s posts, blogs and tweets as you have been on your e-mails and voice mail greetings. For example: “The ABC Agency cannot write, bind or alter coverages or accept claims reports via e-mails or blog posts. If you wish to apply for insurance, you must telephone ABC Agency during normal business hours at 555.555.5555 and speak to an ABC Agency

representative who will assist with your application. To report a claim, you should call ABC Agency at the above telephone number during normal business hours, speak to a claims representative and timely report your claim to us in writing.”

### **Advertising Liability**

Insurance agencies and brokerages have contended for a long time with a host of regulations concerning advertisements that vary state by state. It is imperative that insurance agencies and brokerages follow these regulations when advertising on the social web. Start by contacting your State Insurance Department to see if it has issued any bulletins clarifying the Department’s position on insurance agencies and brokerages advertising on the web.

For example, The New York State Insurance Department has issued Circular Letter No. 5 2001, which provides guidance for New York licensees who advertise on the web. New York insurance agents and brokers should read and heed the entire letter. We wish to highlight the following provisions about delineating advertisements and compensation for non-licensees:

“Internet advertisements for products or services of insurance companies, agents or brokers can appear in many forms, including banners, tiles, hypertext links, frames or embedded links. Such advertisements must be clearly delineated as such and are permitted to appear on the website of a non-licensee even if it leads the consumer to, or is linked to a website where insurance solicitation takes place, as long as the advertisement or website does not include, or the advertisement is not framed by, recommendations, endorsements or promotions from the non-licensee concerning the insurance products or services.

Accordingly, a non-licensee hosting such advertisements on its website may receive compensation calculated in any manner, including flat fees for such advertisements or fees that are based upon the amount of insurance business produced as a result of such advertisements. Advertisements that appear on the Internet are subject to all applicable existing statutory and regulatory guidelines and restrictions applicable to advertisements in any other medium.”

Thus, based upon directives contained in this circular letter, it appears that if you have a non-licensee, such as a trade association, etc., place your agency’s banner and/or a hypertext link to your agency on such non-licensee’s website, it must be labeled as an advertisement and cannot contain any endorsements, etc., from the non-licensee.

### **Suggested E&O Loss Control Prevention Tips**

- It is paramount from both an E&O and regulatory perspective that insurance agencies and brokerages are aware of and follow all of the statutes and regulations pertaining to advertising and how they apply to the social web. A good place to start is with your State Insurance Department. A prudent insurance agent or broker will obtain the advice of an experienced attorney who can help write the agency or brokerage’s policy on web advertising.

## **Conclusion**

Social media networking appears to be a wonderful new tool for insurance agencies and brokerages. Like any tool, it is important that it be used wisely. We hope that the above article will be used by agencies and brokerages as a starting point to consider possible E&O exposures in order to avoid any downside to this fast-growing way of doing business.

## **Disclaimer**

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