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The Fiduciary Duty Of Insurance Brokers In NY

Law360, New York (March 2, 2011) -- On Feb. 17, the New York Court of Appeals issued a long awaited decision in People ex rel. Cuomo v. Wells Fargo Insurance Services Inc., a case that was closely followed in the insurance brokerage industry. The New York attorney general's lawsuit arose from allegations that an insurance broker breached its common law fiduciary obligations to its clients by failing to disclose the contingent commission arrangements it had negotiated with insurance carriers.

In a unanimous opinion, the court disagreed, holding that "an insurance broker does not have a common-law fiduciary duty to disclose to its customers 'incentive' arrangements that the broker has entered into with insurance companies."[1]

Although the ruling's long term impact remains to be seen, the decision is a victory for brokers in New York who now possess a powerful new tool in combating fiduciary liability claims.

The Wells Fargo Decision

The crux of the attorney general's claims in Wells Fargo was that Wells Fargo Insurance Services Inc., an insurance broker, breached its fiduciary duties to its clients, the insureds, by failing to disclose the contingent commissions it received from insurers in connection with its clients' insurance placements.

At the outset, the attorney general faced significant legal hurdles, most notably the Court of Appeals' 1997 decision in Murphy v. Kuhn.[2] Following Murphy, New York courts had long held that, absent exceptional circumstances, the relationship between brokers and their clients is not fiduciary in nature.[3]

Nonetheless, the attorney general asserted that the normal relationship between a broker and insured creates a fiduciary duty because, under New York law, insurance brokers are considered agents of their clients and a fiduciary duty generally lies at the core of every principal-agent relationship.[4]

The attorney general also argued that, while the Murphy decision may have limited brokers' duties in some respects, it did not relieve brokers from a duty of loyalty springing from their status as agents, a duty that should prohibit them from benefiting from undisclosed compensation arrangements with insurers.

In opposition, Wells Fargo cited the long line of New York case law rejecting the imposition of fiduciary duties on insurance brokers absent special circumstances. Wells Fargo's efforts were assisted by the Council of Insurance Agents & Brokers, one of the premier associations of professional brokerage firms in the world, which filed an amicus brief in support of Wells Fargo's position.

Wells Fargo prevailed. Although the court stated that Murphy did not completely exempt insurance brokers from the "general rule that an agent owes a duty of loyalty to its principal," the court held that undisclosed compensation arrangements with insurance companies did not in and of themselves violate any such duty.[5] The court noted the attorney general's failure to allege that Wells Fargo advised clients to buy inferior coverage in exchange for an undisclosed commission or "under the table" payment.[6]

Although the court accepted the general propositions that brokers are agents of their clients and that the principal-agent relationship is fiduciary in nature, the court recognized that brokers, as intermediaries, have a "dual agency status" performing functions for both insurers and insureds.[7]

The court also noted that brokers are very often paid for their services in placing insurance by the insurer. As such, Wells Fargo's collection of contingent compensation was both "commonplace" and merely reflective of "industry custom."[8]

The court's opinion also drew upon the recent implementation of New York State Insurance Department Regulation 194 on Producer Compensation Transparency which requires licensed insurance brokers in New York to disclose contingent compensation arrangements to their clients under specified circumstances.

Recognizing that Regulation 194 administratively established disclosure requirements very similar to those the attorney general argued should be imposed at common law, the court held that a prospective regulation was a "much better way of ending a questionable but common practice than ... creating a common-law rule."[9]

Resolving an issue that has been frequently litigated in New York State, the court concluded that "an insurance broker does not have a common-law fiduciary duty to disclose to its customers 'incentive' arrangements that the broker has entered into with insurance companies."[10]

Potential Significance of the Decision

The Wells Fargo decision will make it very difficult to argue that an insurance broker owes a fiduciary duty to an insured absent special circumstances. It remains to be seen whether future plaintiffs will try to seize on dicta in the case suggesting that a broker does owe a duty of loyalty, albeit something less than a fiduciary duty.

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[1] People ex rel. Cuomo v. Wells Fargo Ins. Servs. Inc., 2011 WL 534198 (N.Y. Feb. 17, 2011).

[2] 90 N.Y.2d 266 (1997). In Murphy, the court held that while insurance agents "have a common-law duty to obtain requested coverage for their clients within a reasonable time or inform the client of the inability to do so ... they have no continuing duty to advise, guide or direct a client to obtain additional coverage." Id. at 270.

[3] See Core-Mark Int'l v. Swett & Crawford Inc., 71 A.D.3d 1072 (2d Dep't 2010); Bruckmann, Rosser, Sherrill & Co. LP v. Marsh USA Inc., 65 A.D.3d 865, 867 (1st Dep't 2009); People ex rel. Cuomo v. Liberty Mut. Ins. Co., 52 A.D.3d 378, 380 (1st Dep't 2008); Hersch v. DeWitt Stern Group Inc., 43 A.D.3d 644, 645 (1st Dep't 2007); Sutton Park Dev. Corp. Trading Co. Inc. v. Guerin & Guerin Agency Inc., 297 A.D.2d 430, 431-32 (3d Dep't 2002)

[4] See N.Y. Ins. Law § 2101(c).

[5] People ex rel. Cuomo v. Wells Fargo Ins. Servs. Inc., 2011 WL 534198 (N.Y. Feb. 17, 2011).

[6] Id.

[7] Id.

[8] Id.

[9] Id.

[10] Id.