



# Packing Their Parachutes

Advising Clients About Business Insurance Coverages

By Michael S. Hale and Melissa L. Hirn

**I**n many ways, good business lawyers are parachute packers, spending countless hours trying to protect their clients from free falling by carefully drafting documents, forming entities, and advising on employment liability preventive measures, among other things. Yet a client's commercial insurance program may be the final word on managing a particular loss exposure given the transfer of risk to the insurer. Is that insurance program sound? Has it been designed by an insurance agent who is an order taker rather than an advisor?

Lawyers often overlook great opportunities to create unique value with their clients by asking some basic questions about insurance protection. This is something many accounting firms are already doing. Nonetheless, many lawyers shy away from advising clients on insurance gaps, probably because they either believe they don't have knowledge of the policies or are concerned about liability. However, if the business lawyer completely sidetracks all insurance discussions, he or she may do a disservice to the client and, in the process, incur potential personal liability.

There is, no doubt, a close link between commercial insurance and the lawyer's other mitigation-of-risk work such as drafting leases and contracts. This article provides some tips in this all-too-often ignored area of practicing law.

## Your client's business insurance gap could become *your* problem

### Scenario one

You learn on the news one morning that your client's multimillion-dollar commercial office building has burned,

leaving the business in a state of crisis. The leases you drafted contained insurance requirement provisions, but also included a section allowing the tenants to terminate the lease if more than 50 percent of the building was damaged. It is an especially bearish real estate market and your client is concerned about finding new tenants once the building is rebuilt, which will take approximately 18 months considering ordinance issues. Your client calls you to ask for advice. After all, *you* wrote the lease agreements. You are a business attorney with little knowledge of insurance coverages or insurance law. Is this an opportunity to shine in front of the client, who provides significant revenues to your firm, or should you punt?

### Scenario two

You have advised your manufacturer client that it can limit liability by forming separate limited liability companies for the real estate it owns and its two separate business divisions. The client agrees, and you form these entities. Later that year, a lawsuit is filed in which all three entities are named as defendants. The client then becomes aware that the insurance agent had listed only the main entity on the general liability and umbrella policies and not the other two divisions. You believed that the client would alert the insurance agent or the agent would ask the right questions, neither of which occurred. After the client gets the denial letter from the insurer, she asks you why there is now more exposure to her with this entity structure. Do you advise her that insurance is outside the scope of your services or divert blame to the agent? Could you have done anything to prevent this scenario?

## fast facts

- Most companies look to qualified law firms to manage their business legal risks. More often than not, however, attorneys pay less than adequate attention to uncovering potentially calamitous insurance coverage contract issues for those same clients.
- Many businesses buy policy contracts sight unseen and typically do not treat insurance policies with the same level of scrutiny as other contracts. This is an anomaly for lawyers who are used to negotiating contract language up front and may put the client in a precarious position, particularly given the limited role of many insurance agents.
- A checklist on the following page illustrates some of the major coverage problems that could be affecting your clients, which they may not otherwise find out about until a claim occurs.

Similar scenarios are all too familiar to many law firms. While there are fine lines between talking with clients about insurance coverage issues and undertaking the role of an insurance consultant, to properly do his or her job, the business lawyer effectively has little choice but to discuss the topic of insurance. In doing so, there are often great opportunities to add value to the attorney-client relationship.

### The insurance agent's limited role creates opportunities for law firms

While many agents cavalierly define "great service" as how quickly they return calls or reply to e-mails, the more proficient agents judge themselves on how well they advise their clients on the coverages, and strive to be more than mere order takers. Insurance agents, who are often at the center of protecting a company's assets, are only required to take a 40-hour self-study course followed by an examination to be able to legally sell insurance in many states, including Michigan.<sup>1</sup> Agents are sued for errors or omissions more often than many might think.

Michigan courts have gone as far as to identify insurance agents as having a limited role.<sup>2</sup> The law distinguishes insurance agents from insurance counselors, expressly restricting the former from providing "advice, counsel, or opinion with respect to benefits promised, coverage afforded, terms, value, effect, advantages, or disadvantages of a policy of insurance" except for advice which insurance agents customarily provide.<sup>3</sup> Interestingly, unlike insurance agents, attorneys don't have to be licensed as insurance counselors to engage in these evaluation services.<sup>4</sup>

In most states, including Michigan, the independent insurance agent is the legal agent for the insured, meaning any misrepresentation by the agent likely will not bind the insurer.<sup>5</sup> To add to the quagmire, the general rule in Michigan is that the insurance agent owes no duty to advise on the adequacy of coverage, with certain exceptions.<sup>6</sup> This creates major issues

for clients who may be left with the sole remedy of suing the agent for an uninsured or underinsured claim.

The limited role of the insurance agent triggers potential opportunities for lawyers to create value, distinguish themselves from other firms, and develop revenue by making some threshold suggestions to the client. Perhaps most importantly, this could help save the client from a catastrophic uninsured or underinsured event.

### Your firm's unique value in discussing insurance issues with clients

It is surprising how infrequently law firms raise insurance coverage gaps, much less ask to review their clients' business insurance policies. Accounting firms are more likely to ask questions and talk with their clients about matters such as business interruption coverage and related issues.

Practitioners can build value with their clients by doing five basic things relating to their clients' business insurance:

- (1) Ask some threshold questions about insurance to trigger discussion.
  - a) Develop a named insured grid that lists all entity names related to the business and have your client ask its agent to check off which names are covered under what policies, including general liability, umbrella, employment practices, workers' compensation, automobile, etc. You may be surprised at the gaps you will find, and you could look like a hero to your client for uncovering these issues pre-loss.
  - b) In the first scenario we discussed previously, if the agent had not negotiated an extended period for continuing the loss of rents after the building was rebuilt, the client could be irreparably damaged. The same goes if proper ordinance coverage had not been negotiated. Ask your client about these basic underlying exposures.

- c) One of the telltale signs of trouble is if there are co-insurance provisions on your client's property insurance policy. Ask your client to check with the agent about this. If a provision exists, your client could have a major potential exposure, and this may be a red flag concerning the agent's competence.

Of course, these are only a few talking points. A checklist of some of the other coverage problems we often

find in business insurance programs is included below and could be an additional tool for the business lawyer.

- (2) Make the insurance agent a part of the overall team of advisors for the client after evaluating the agent and agency for competence. If the agent presents himself or herself as an order taker instead of an advisor, it may be time for a new agent for your client.

## Common Business Insurance Coverage Oversights

### General Issues

1. Entities are listed inconsistently among various policies.
2. Client does not complete the application.
3. Leases do not track insurance coverages.
4. No waivers of subrogation negotiated.

### Property Insurance

1. Building and contents limits are based on book value or otherwise inadequate.
2. Blanket limits not negotiated.
3. Dangerous coinsurance penalty provisions not removed for buildings or contents insurance.
4. Personal property of others not properly covered.
5. Foundations coverage not included.
6. Inadequate coverage for increased costs of construction from ordinances.
7. Business interruption coverage on a coinsurance basis.
8. No extended period of indemnity negotiated beyond 30 days.
9. Protective safeguard provisions not removed.
10. Water damage exclusions/absence of flood coverage.
11. Triple net leases—listing landlord as loss payees rather than additional insureds.

### General Liability Insurance

1. Contractual liability coverage limitations exist.
2. Additional insureds not included.
3. Broad form notice of occurrence not included.
4. Employee benefits legal liability not included.
5. Personal and advertising injury exclusions.
6. Aggregates per location or project not negotiated.
7. No waiver of subrogation negotiated with insurer.
8. Designated premises limitations limit coverage.

### Business Automobile Insurance

1. Broadening endorsements not negotiated.
2. Employee as additional insureds not included.
3. Supplementary personal injury protection endorsement not included.

4. Vehicles owned or leased by members not properly addressed in business auto policy.
5. No coverage for damage to rental cars.
6. No lease gap coverage.

### Umbrella Liability Insurance

1. Named insureds not the same as listed on the general liability insurance policy.
2. Umbrella has endorsements making it less broad than the underlying policies.
3. No pollution exclusion carve-backs.
4. Cross-suit exclusions.
5. Employee benefit legal liability not scheduled.

### Management Practices Insurance

1. Third-party employment practices not included.
2. No coverage for wage-and-hour violations.
3. Immigration violation coverage not included.
4. No fiduciary liability coverage negotiated.
5. No carve-backs on D & O for insured vs. insured exclusion.
6. No cyber liability coverage purchased.
7. No contingent business interruption cyber liability coverage purchased.

### Crime Insurance

1. Third-party employee dishonesty coverage not included in crime policy.
2. No cyber extortion coverage included.
3. No social engineering coverage included for phishing-type claims.
4. Inadequate coverage for claims expenses to prove loss.

### Professional Liability Insurance

1. Contingent bodily injury and property damage not included.
2. Named insureds missing.
3. Insured vs. insured exclusions.
4. Definition of professional services too narrow.

*As parachute packers go, lawyers can do a tremendous service to their clients by offering some basic direction related to a critical part of the overall business's legal risk-management strategy—the client's insurance policies.*

- (3) Consult with the agent and other insurance experts about insurance requirement provisions *before* the contract or lease you drafted is executed. Often, if the agent is given copies of the leases or contracts at all, it is only after they are in force, rendering any necessary changes in coverage unlikely.
- (4) Recommend insurance coverage counsel or insurance consultants to your client to provide objective advice on competing brokers, policies, and pricing.
- (5) Consider lawsuits and administrative actions against your clients such as Equal Employment Opportunity Commission (EEOC) or Department of Labor investigations as events that could trigger insurance. Be certain that the client is advised to report these claims to its respective insurers. Too often, law firms respond to EEOC Notices of Charge of Discrimination for their clients, and in doing so, may be voiding coverage under the client's employment practices liability insurance policy.

**The scope of services in an engagement letter should either explicitly include or exclude insurance issues**

A well-drafted engagement letter should either explicitly include or exclude duties related to the design of the client's insurance program, the submission of claims to insurers, or the recommending of specific coverages.

Even though an attorney should have some involvement in the insurance program of the business client, some things should probably be avoided as a matter of course:

- Completing proof-of-loss forms or valuing claims
- Accepting notice of claims from clients to report to insurers
- Negotiating renewals directly with the client's insurance agent
- Settling liability claims within a client's self-insured retention without consent from the client's insurers
- Advising of the availability or unavailability of coverage for a specific exposure.

## Conclusion

Most parachutists do not complain if their parachute fails to open; it is usually too late. As parachute packers go, lawyers can do a tremendous service to their clients by offering some basic direction related to a critical part of the overall business's legal risk-management strategy—the client's insurance policies. ■



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## ENDNOTES

1. MCL 500.1204(a).
2. *Deremo v TWC & Assoc, Inc*, unpublished opinion per curiam of the Court of Appeals, issued August 30, 2012 (Docket No. 305810).
3. MCL 500.1232; see MCL 500.1234, MCL 500.1236.
4. *Id.*
5. *Plitt et al, Couch on Insurance* (3d ed), § 45:5; *Genesee Foods Services, Inc v Meadowbrook, Inc*, 279 Mich App 649, 654; 760 NW2d 259 (2008).
6. *Harts v Farmers Ins Exch*, 461 Mich 1, 6; 597 NW2d 47 (1999).