Agents & Brokers

Colorado Appellate Court Rejects Intermediary's Intentional Interference with Prospective Business Relations and Breach of Fiduciary Claims Based on Manner in Which Insurer Adjusted Claims

Insurers Did Not Owe Intermediary Fiduciary Duties

MDM Group Associates, Inc. v. CX Reinsurance Company LTD., U.K., ___ P.3d ___, 2007 WL 528800 (Colo.App. 2007)

Case at a Glance

An insurer guilty of poor adjustment practice is not liable to an intermediary for intentional interference with prospective business relations, even if the insurer's conduct causes an entire insurance market to disappear for the intermediary. Insurers are not fiduciaries of intermediaries, and therefore an intermediary can not state a claim against an insurer for breach of fiduciary duty.

Summary of Decision

MDM Group is an insurance broker. Its president developed a novel insurance idea. He designed an insurance program for insuring ski resorts against the risk that the number of "paid skier days" during a given ski season would fall below a specified number. The program was designed so that it could fit other types of resorts when they lost "paid *X*-type days."

The program worked well for sky resorts for two years and caught-on big-time in the third year. There were no claims in the first-two years, since it snowed a fair amount. In 1999-2000—the third year--the program grew by 500%. After the 1999-2000 season, all of the insured resorts submitted claims. CX was the only insurer. It "negotiated, mediated, and litigated the claims, ultimately paying in excess of $23 million to complete and settle them" CX declined to renew any policies after the expiration of the policies in May 2000.

As its first cause of action, MDM sued CX for intentional interference with prospective business relations. It contended that CX's claims bad faith handling practices undermined the market for "lost paid skier days" insurance. MDM maintained that its existing customers' bad experience with CX caused them not to seek replacement coverage with another insurer, which caused MDM "to lose renewal commissions." MDM's claim extended beyond those who had already purchased insurance; MDM alleged that news of CX's poor claims handling practices discouraged potential new clients from purchasing similar policies from CX or any other insurer. MDM also alleged that CX owed it a fiduciary duty, since CX was the principal in an agency relationship with MDM.

The case was tried to a jury. It found in favor of MDM for $6,750,783 in damages, and the trial court later awarded more than $1million in prejudgment interest. The trial court had dismissed a claim for punitive damages.

On appeal, CX raised two separate issues. First, it contended that the judgment based on the intentional interference with prospective business relations had to be reversed for a variety of different reasons. Second, it contended that it was not a fiduciary with respect to MDM, although MDM may have been a fiduciary with respect to it.

Intentional Interference. CX attacked the intentional interference portion of the verdict and judgment on six separate grounds. The court of appeals considered only one of them, agreeing with CX that MDM would not have been a party to any prospective contracts.

To be sure, said the unanimous court, Colorado recognizes the tort of intentional interference with prospective business relations, as set forth in §766B of the RESTATEMENT (SECOND) OF TORTS (1979). This section makes actionable the conduct of a person who "intentionally and improperly" interferes with another's prospective contractual relation[s]." Given the way courts have interpreted this rule, "[i]nterference with another's prospective contractual relation is tortious only if there is a reasonable likelihood or reasonable probability that a contract would have resulted." At the same time, of course, a party cannot be liable for interfering with its own contract. In other words, if the person or entity is a party to a contract, it cannot interfere with that contract.

This created an interesting legal question. With what contract was MDM alleging that CX interfered?

There appeared to be two alternatives. The first was whatever contract there was between MDM and CX. The second was an entire group of contracts MDM alleges it was going to have with resorts (and similar entities) which would have purchased insurance through it. See *Sterling Colo. Agency, Inc., v. Sterling Ins. Co.*, 266 F.2d 472 (10th Cir. 1959).

Of course, a party cannot, as a matter of tort law, interfere with a contract with respect to which it was a party; it can only breach it. Therefore MDM cannot succeed against CX by claiming that CX interfered with the prospect of a contract to which CX would have become a party. This would exclude from consideration (1) any contract CX might come to have had with MDM itself, and (2) any insurance policy CX might have issued to any prospective insured. Thus, MDM must be asserting that the relationships actionably interfered with is "the prospective or future contractual relationship[s] between it and [various] ski resorts and [other] prospective insureds such as the North American Japanese Ski Resorts[.]"

The court, however, rejected MDM's gambit because MDM, as insurance intermediary, was not a party to any contract with the insured. Instead, MDM's role was limited to helping the insurance company procure and service that company's contract with the insured. The insurance intermediary, therefore, is but an "'incidental beneficiary to the contract between the insured and the insurance company. The agent's rights to commissions—his economic interest in the insurance contracts—is of no concern to the insured, and solely a matter of contract between the agent and his principal, the insurance company.'" See *Shrewsbery v. Nat'l Grange Mut. Ins. Co.*, 395 S.E2d 745, 748 (W.Va. 1990).

According to the court, MDM therefore had no prospective contracts with any potential insured, since it would always be acting as an agent for the underwriter insofar as it was procuring insurance. "Indeed, the evidence here showed that MDM received commissions on these particular policies from AON, an intermediary broker, who in turn received commissions from CX. No insured entity paid commissions to MDM, and the evidence did not show that any future potential insureds would do so either."

In the alternative, MDM asserted that even if there was no contractual relationship between it and an insured, for whom it procured insurance, there was a quasi-contractual relationship, and by fouling up the insurance market, CX had interfered with prospective quasi-contractual relationships. The court rejected this argument, for reasons similar to the reasons it rejected the interference with prospective contract argument. To be sure, if CX were to issue insurance policies to insureds in the future as the result of MDM's efforts, MDM's rights would "devolve from the obligation of the insurer to compensate its agents. Hence, MDM would have no prospective quasi-contractual relations with insureds or potential insureds[.]"

Thus, because MDM could not and did not present any evidence of any prospective contractual or quasi-contractual relations with any ski resorts, its tortious interference claim failed. Therefore, CX was entitled to directed verdict on the prospective tortious interference part of the case.

Fiduciary Duties. This claim too failed. Generally speaking, "a principal does not owe a fiduciary duty to an agent as a matter of law." Agents owe principals fiduciary duties, but—generally speaking, at least—not vice versa. Obviously, "[t]he existence of a fiduciary relationship is a prerequisite to finding of a breach of fiduciary duty." Usually, when there is a fiduciary relationship, the fiduciary duty runs in one direction, it runs from attorney to client, not from client to attorney. It runs from trustee to beneficiary, not from beneficiary to trustee. Usually, it runs from agent to principal and not from principal to agent. There are exceptions to this general rule. Partners can owe each other fiduciary duties. No such exception applied here.

In general, fiduciary duties arise (a) when one party has a significant degree of control over the property or subject matter of another, or, (b) they arise when the party receiving the benefits places a high degree of degree of trust and confidence in the other. It is the placement of a high degree of trust and confidence that gives rise to fiduciary duties. A fiduciary is supposed to look out for the best interest of the cestui, whose interests the fiduciary must place ahead of his own. "In the principal–agent context, it is the *agent* who owes a fiduciary duty to the principal as a matter of law." To be sure, "[a] principal does owe *some* duties to an agent." However, these obligations are not those of a fiduciary. See *Restatement (Third) Agency* § 1.1 cmt.e, (2006). Interestingly, the court of appeals reviewed the jury

instruction given by the judge. They found that the jury was wrongfully instructed that the principal owes the agent fiduciary duties. "As a matter of law, a principal is not a fiduciary of an agent. The principal is not 'entrusted to act for the benefit of or in the interest of another.' It is the principal who entrusts business to the agent to act for the principal's benefit. Any duty owed by a principal to an agent is not fiduciary." Consequently, CX was not the fiduciary of MDM, and if it breached obligations it had to MDM, they were not fiduciary in nature.

Comment

The court's discussion of fiduciary duties seems straightforward and uncontroversial. What is striking about this case is that the court believes that no contractual relationship ever forms between insurance intermediaries and those who are buying insurance through them. Can this be right? Suppose an intermediary promises a customer to obtain two policies of insurance for it—say, a CGL and an umbrella policy—but fails to purchase the umbrella policy. Isn't that a breach of contract? (This hypo is based on another case discussed in this very issue, *Terrain Tamers Chip Hauling, Inc. v. Insurance Marketing Corporation of Oregon* .) The only way to say that it is not is to say that there is no consideration involved. That is precisely the position of this court of appeals. It reasons that since the commission comes from an insurer or from a wholesale broker, it does not come from the customer of the intermediary. There are two comments to make here. First, all the money for the premium comes from the customer (or from its financing agency). Just because it flows through other sources does not eliminate the real source. Second, many times premium comes from the insured and goes to the intermediary; it deducts what is owed it; and the money is then passed on to the insurer or the wholesale broker. The idea there are never contracts between insureds-to-be and insurance-intermediaries is clever but absurd. // Quinn