



Alaska Conference Call July 27, 2017

Rice Insurance Services Company, LLC (Rice) is an agency formed by our family exclusively to administer Real Estate Errors & Omissions (Real Estate E&O) insurance through mandated group programs. The Rice family and employees of Rice have been involved in the establishment and administration of mandated programs for many years, beginning in 1989. We are the current group provider in eleven of the thirteen states that offer a group program and require all active real estate licensees to maintain insurance. (LA, CO, ID, IA, KY, MS, ND, NM, SD, TN, RI) (not NE WY but we write an independent program in NE). Alaska will be the 14th state to have a mandated program and offer a group policy in 2018.

We are an insurance agency and administrator located in Louisville, Kentucky. Administering group programs for mandatory E&O states is our only business. We administer programs for real estate licensees, appraisers and were recently awarded a contract for mortgage loan originators in Colorado which is regulated under the Division of Real Estate. We do not write any other insurance programs. Another important factor that sets us apart from other insurance agencies is that we also handle claims in-house for the group programs we provide. Rice is staffed with 11 in-house claims specialists, 8 who are also attorneys, to oversee and adjust claims submitted under our real estate E&O programs. These in-house claims specialists allow us to provide specialized knowledge in claims handling, as well as a higher level of service when an insured is faced with a claim.

When an insured calls Rice with a question about coverage, they will be speak directly with one of our on-site claims specialists. These are the very same individuals that receive claims and are involved in the initial coverage determination. When a covered claim needs defense counsel, we will assign the matter to an Alaska attorney. The insurance carrier for our programs, CNA is currently working to help create a list of Alaska legal firms to handle claims under our program.

Unlike many agencies, we work with only one insurance carrier in the mandated programs. Our partner for the mandated programs is Continental Casualty Company, one of the CNA companies. CNA is the number one provider of real estate liability insurance in the U.S. Its nationwide data helps us to identify trends in business and provide expert claims support on a broad number of real estate liability issues. We have partnered with CNA since 2001.

Rice was awarded the contract to administer the Alaska group program. We are excited about working with the Alaska Real Estate Commission, the Association of Realtors and the Alaska licensees. I am here today to provide some information on mandated insurance programs, an update on the program for Alaska and to answer any questions.

We are happy to be able to offer this group program with affordable coverage and valuable protection for the majority of licensees. Unfortunately, a licensee can sometimes do everything by the book, but still find themselves faced with a claim when something goes amiss. Our society is becoming more litigious, and this trend creates increased likelihood of a claim, even if the licensee has done nothing wrong. A claim can be disastrous from a financial, mental, and professional standpoint. Having adequate insurance protection is invaluable.

In some states, real estate licensees are unable to find any affordable coverage. Some licensees (particularly those who have had prior claims) may not even be able to find a company willing to provide a quote for E&O coverage. Since the group program MUST accept all active licensees and there is a maximum fixed premium for the basic policy, the mandated program assures that E&O insurance is available and affordable to all Alaska licensees.

We received the Alaska contract award on July 13, 2017 (the Notice of Intent to Award was issued on June 13). We will be offering the program effective 1/1/2018. Some people have asked if we will be offering the program early and we have been able to do that in some states. Once the program has been finalized and filed and approved by the insurance division, we may be able to do so, if the State would like for us to do so.

There were two bidders for the Alaska program. The Invitation for Bid requested that bidders include a minimum premium and a maximum premium. Our minimum premium was \$450 and the maximum \$642. The other bid's minimum premium was \$747 and the maximum premium was \$2,234 (the other bid was submitted by Insurance Brokers of Alaska – the carrier was Hiscox Insurance Company, Inc.) Note that our maximum premium was less than the other bidder's minimum premium and both of our premium amounts were significantly less than the other bidder's maximum.

Let's look at our program's premium amounts.

The **minimum premium (\$450)** is Premium Level A – it is a discounted premium for licensees who exclusively perform Residential Sales and have had no claims in the past 5 years. **Residential Sales** means sales of properties of four families or less, zoned for and occupied exclusively as residences. Vacant land sales shall be considered residential sales, provided the land is zoned for residential use and is not a development project of four or more homes. Sales that involve farm property where a buyer would derive no more than 25% of total income from farming and where it is a buyer's principal residence are considered residential sales. Residential sales do not include rental, leasing, appraisal or other non-sales activity involving residential property)

The **maximum premium (\$642)** is Premium Level B – it is for licensees whose professional services include commercial sales, property management and/or community association management. It is also for licensees who have had a claim in the past 5 years. In the event that a licensee has performed these types of transactions in the past, is currently performing these types of transactions, or expects to perform them in the future, the licensee should pay Premium Level B (the maximum premium). The licensees who pay the minimum/discounted premium will not have the endorsement attached to the policy to insure claims involving non-residential transactions. Licensees who are involved in non-residential transactions will need to have the endorsement insuring non-residential transactions at the time of the transaction. In addition, since the policy is a claims made and reported policy, the policy that is in effect at the time of the claim will need to have the endorsement attached in order for coverage to apply to the claim.

We are currently working on the insurance policy form with the insurance carrier and will be filing it with the insurance division once the review by CNA's legal division has been completed.

Let's go over some information regarding the mandated program.

HOW DOES THE MANDATED PROGRAM WORK?

In a typical state-mandated E&O program, an "official" insurance carrier is designated by the state's Real Estate Commission or Regulatory Board. That carrier must make coverage available to EVERY real estate licensee in the state. The insurance company cannot exclude anyone - the coverage must extend to both low risk and high risk licensees - so there is no underwriting. This is a guaranteed- issue, fixed premium basis per licensee. In Alaska, there will be two premium levels.

Individual licensees are required to either obtain insurance from the "official carrier" or provide proof of other insurance coverage that satisfies the requirements of the Commission and applicable state laws.

NOW LET'S TALK ABOUT THE "OFFICIAL POLICY".

The policy of the official carrier in the mandated states is an "INDIVIDUAL policy". Traditionally, real estate E&O coverage has been in the form of a "FIRM policy". The firm usually paid a premium based either on the number of transactions per year, or based on the amount of commissions earned per year. The firm policy would cover anyone in the office who may be involved in a real estate transaction.

The firm policy can be problematic for a licensee who switches from one firm to another, leaves the firm to enter into another line of work or simply leaves the firm for other reasons. The "firm policy" may not protect the former licensee if it only covers persons who are actively engaged in the operations of, or employed by, the insured firm at the time the claim is made. Also, if the firm drops coverage or moves its coverage to a company which does not cover prior acts, the individual licensee may be left unprotected.

With the individual policy, when the licensee moves from one firm to another, the policy travels with the individual licensee and covers BOTH the licensee and the firm. The policy will cover any firm or employer of the licensee for its vicarious liability for the errors and omissions of the covered licensee. When I use

the term "vicarious liability" here, I mean legal liability which is attributed to the firm for the acts of its licensee.

Even if the agent has moved to another real estate firm at the time the claim is made, the individual policy will travel with the agent. It will cover both the licensee and the present firm for acts of the licensee while at the present firm. It will also cover both the licensee and the former employer for acts of the licensee while at the former firm (this is true even if the claim is made after the licensee has switched firms). Of course, this is only true if the agent maintained continuous coverage from the time of the error or omission until the claim was made.

When reviewing an insurance policy, licensees should ALWAYS review the definition of who is an insured. Under the group policies that we administer, the Real Estate Firm is listed in the definition of Insured. If there would be coverage for the insured licensee under the terms of the policy, then the definition of Insured will also include any Real Estate Firm or real estate franchisor that the **Licensee** represents but only for its vicarious liability for negligent acts, errors, or omissions in the **Licensee's Professional Services**.

Now we understand how an individual policy works – let's take a look at the "claims-made" aspects.

THE "OFFICIAL POLICY" IN MANDATED STATES IS USUALLY A "CLAIMS-MADE" FORM.

The insurance policy is written on a "CLAIMS-MADE" basis. This means that coverage is provided only to those CLAIMS that are MADE (that is brought) against the licensee for acts or omissions that occurred during the time the policy is in force.

Occurrence vs. Claims Made Policies

Some policies are written on an Occurrence base. Your homeowners and auto insurance are Occurrence policies. The policy that applies to the claim is the one in effect when the damage or accident occurred.

- ❖ Real estate E&O insurance policies are claims-made and reported.
- ❖ Under a claims-made policy, the policy that applies is the one in effect when the claim first arises, NOT the one in effect when the transaction occurred.
- ❖ For a claim to be covered under a claims-made policy, the insured is typically required to have coverage in place on the date the claim is made, and continuously without interruption back through the date of the acts underlying the claim.
- ❖ Under most claims-made and reported policies, there are 4 important dates.
 1. The policy's retroactive date (under our policies, this is the date the licensee first obtained, and since which has continuously maintained, E&O coverage),
 2. The date of the professional services giving rise to the claim,
 3. The date the claim is made (claims often arise years later, so Tail Coverage should be considered if inactivating license), and
 4. The date the insured reports the claim to the insurance company.

Generally, for a claims-made and reported policy to apply to a claim, the insured must

1. Be insured under the applicable policy or an extended reporting period on the date the claim is made,
2. Have had real estate E&O insurance on the date of the professional services giving rise to the claim,

3. Performed the subject professional services on or after the policy's retroactive date (under policies issued by RISC, this requires the insured to have continuously maintained real estate E&O insurance between the date of the professional services and the date the claim arose), and
4. Timely report in accordance with the applicable policy and state law.

Generally, real estate E&O insurance applies to claims alleging negligent acts, errors, or omissions in the insured licensee's professional services (read the policy or contact the provider to determine what are considered professional services under the policy).

WHAT IS A CLAIM?

Sometimes it's obvious a claim has been made, for example, if a licensee is served with a lawsuit.

However, sometimes it may not be as clear. A claim can also be a written demand for money or services received by the insured that alleges a negligent act, error, or omission regarding professional services.

That means an email, fax, or letter accusing a licensee of doing something wrong may arise to a claim.

WHAT ARE THE LIMITS OF LIABILITY FOR THE MANDATED COVERAGE?

The limit of liability for mandated coverage is \$100,000 each claim. Different insurance companies treat their limits of liability differently. For example, our programs do not include the cost of defending claims in the \$100,000 limit of liability. All legal expenses and other costs to defend are IN ADDITION TO the policy limits and are not included in determining whether limits have been met.

Some insurance companies include legal expenses and other costs to defend as part of the liability limit. Which brings us to an interesting point. Our claims history has shown that legal expenses often cost two to three times as much as loss expenses paid in judgments or settlements. Since legal expenses are generally far greater than loss expenses, the different treatment of legal expenses can cause an enormous difference in determining a policy's true liability limit.

The group policy in Alaska will offers \$100,000 coverage with \$300,000 annual aggregate (this is the most that the insurance company will pay for all claims against the licensee during the annual policy period. The deductible will be \$2,500 for damages (meaning payments made for a compensatory award or settlement). There is NO DEDUCTIBLE for legal fees.

What happens if you are sued for \$250,000? The insurance company will defend the claim but reserve rights to deny the claim for any judgment amount over the \$100,000 limit per licensee. If a judgment is rendered in an amount over the \$100,000 limit - then the policy will not pay any amount over the limit.

In our experience, we have seen very few claims where there was a judgment against a real estate licensee for more than \$100,000. We see quite a few claims where the claimants ask for more than \$100,000 in the lawsuit. Often there are several parties alleged to have liability and often other parties (such as the seller, the termite inspector...) have the bulk of the liability and the real estate licensee's share of the final judgment is relatively small.

There will be an excess program available for firms who would like to purchase limits up to \$1 Million over the basic policy limits. In order to obtain a quote for firm excess coverage for your firm, the principal broker must complete an excess coverage application and send it to in for review. Please note that for our programs, the excess policy may only be issued if all of the firm's licensees possess and maintain coverage pursuant to the underlying group policy issued by Continental Casualty Company.

CLAIMS HANDLING AND SETTLEMENT

We have a lot of experience handling E&O claims. In 12 states with mandated group programs, Continental Casualty Company has paid more than **\$117,705,000** since 2003 for damages and claim expenses on behalf of licensees insured by our programs (in addition, there is more than \$10,800,000 currently set aside in reserves for open claims at June 30, 2017.) Our claims staff works with the insured

licensee and outside legal counsel to handle the claims for our programs. We had a question submitted about claims settlements. The policy provides:

The Company will not settle any **Claim** without the consent of the **Insured**, which consent shall not be unreasonably withheld. If the Company recommends a settlement to the **Insured**, which is agreeable to the claimant, and the **Insured** does not agree to settle, then the Company's applicable Limits of Liability are reduced to the total amount for which the **Claim** could have been settled. The maximum amount the Company will pay in the event of any later settlement or judgment is the amount for which the **Claim** could have been settled plus the amount of **Claim Expenses** incurred up to the time the Company made the recommendation, less any applicable deductible.

Our claims handlers are experienced and do not recommend settlement unless there is liability or a possible finding of liability and it is in the best interest of all involved.

NOW THAT YOU UNDERSTAND HOW THE PROGRAM AND POLICY WORK, HOW DOES A LICENSEE ENROLL IN THE PROGRAM? We will send an enrollment form to all licensees. The enrollment form will explain how to select the correct coverage and premium amount. The form is being finalized but the current draft has 2 questions for the licensee to respond Yes or No and follow the schematic for selecting the proper premium.

DETERMINE SCOPE OF COVERAGE – Mark Yes or No as applicable. The AREC will be notified of false reporting of your real estate activity or claims history on this form.

Question 1.

Have you had any Paid Claims in the past 5 years?

Paid Claim is (1) a written demand for money or services or (2) service of a lawsuit or institution of arbitration or mediation proceedings that seeks Damages and alleges a negligent act, error, or omission in your Professional Services as a real estate licensee, in which payment was made for Damages (compensatory award or settlement) or Claim Expenses (legal fees/defense costs) by you or on your behalf.

Question 2.

Do you, have you ever, or do you plan to do real estate activity other than Residential Sales?

Residential sales are (1) properties zoned for and occupied exclusively as residences for 4 families or less; (2) vacant land, provided the land is zoned for residential use and is not a development project of 4 or more residences; and (3) farm property that will be a buyer's principal residence and where a buyer will derive no more than 25% of total income from farming. Residential Sales do not include commercial sales; commercial listings; or renting, leasing, managing, or appraising any type of property.

If the licensee selects YES to either of these questions, then they MUST select the enhanced coverage option (Premium B \$642)

If the licensee selects NO to both questions, then the form asks:

Do you want insurance for any and all professional services that require a real estate license, including (a) sales or listings of all types of property, not just those zoned for and occupied exclusively as residences for 4 families or less; (b) renting, leasing, managing, or appraising any type of property, including residential; and (c) community association management?

If the licensee selects Yes, then they may select the enhanced coverage option (Premium B \$642). If the licensee selects not, then they may select the Residential Sales Coverage Only (Premium A \$450)

We should have the policy forms and enrollment forms ready soon for review by the Commission. We are pleased to partner with the Alaska real estate commission in providing this valuable program for real estate licensees. Thank you for the opportunity to talk with you today. At this time, I would like to open the floor for questions or any issues you'd like to address.