

Commentary***Letter To A Reinsurance Friend******(Reinsurance Claims Handling In A Nutshell)***

By
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Dear John,

So you took the plunge. You quit that stuffy old law firm and accepted a senior claims job at Total Reinsurance Company. Congratulations. I wanted to be among the first to wish you luck. When we spoke yesterday, you asked me to give you some suggestions on what to do in your new claim job at a big reinsurance company. I am flattered you asked and happy to oblige but I can only give you my two cents — you'll have to judge things for yourself when you get there. After you have gotten your feet wet at the company, read this again and let me know how close to the mark I was.

First things first. Being a claim representative of a big reinsurer is fun. You will be exposed to a diversity of claims: everything from auto cases to medical malpractice to D&O claims to major property losses to environmental (asbestos, hazardous waste, etc.) Most of these claims will be large and complicated and will require your detailed analysis. You will travel to many parts of the country and see how a wide variety of insurers and self-insureds handle their claims.

Cedants will view you differently depending on the size of the company you visit. To the small companies, you will be an all-knowing visionary whose every word is inspired. To the large companies, you will be an annoying pest.

Keep in mind, also, that things are changing in the insurance and reinsurance world. The whole industry is consolidating into fewer and ever larger companies (think Berkshire Hathaway purchasing General Re and Munich Re acquiring American Re.) And now the line is blurring between insurance and reinsurance products. There are lots of reasons for this including cedants' flight to quality and reinsurers' need to achieve economies of scale. If they hired you at Total Re, I would say they really, really needed you. There are no extra bodies hanging around the offices of insurers or reinsurers anymore.

Second, at Total Re you will not be a claims person at all. Not really. They may call you that, but don't believe it. You will not interview witnesses, photograph accident

scenes, take statements, depose experts, or supervise counsel. The claim staff at the ceding company does all of those traditional claim tasks. Instead, at Total Re consider yourself part of underwriting, treaty production, actuarial, and accounting all at the same time with a sub-specialty in the claims field. Your true role at Total Re is to work within each of these departments and to bring to light the claims issues that affect these groups.

Let's take them one by one.

1. Underwriting. Total Re's goal is to make money reinsuring its cedants. It wants to pick the right companies and charge the right price. That is an underwriting function. To do this, the Total Re underwriting department will examine the business to be reinsured and structure a program. How the program is structured depends largely on the degree of risk that the underwriter sees in the transaction.

To weigh the risk, the underwriter will need to know, among other things, how well the cedant's claim department shapes up in comparison with others. Does it have enough people? Are they competent? Do they do a good job in investigating, reserving and settling their cases? How quickly will they report claims to their reinsurer?

The Total Re underwriters are interested in these things because they affect the adequacy of the rate charged the ceding company. This is where you come in. The poorer the quality of the cedant's claim handling, the higher the rate must be to make up for the riskiness this deficiency creates. The better the quality, the less risk and the lower the price can be. Of course, if the claim handling is extremely bad, no price will ever be adequate to cover the losses.

As a claim person, you can also shed light on the kinds of exposures the underwriters should expect on a specific book of business. Tell the Total Re underwriters about the types of claims that will arise, the trends in values, as well as important coverage issues. Anecdotes are instructive. Provide lots of examples. This will give them concrete knowledge and allow them to more profitably structure the reinsurance program.

If there are problems in the cedant's claim department, you will need to make suggestions for improvement so that the cedant *and* Total Re can improve their bottom line.

At Total Re, you will really be a part of the Underwriting Department.

2. Production. To the ceding company, you are the day-to-day face of Total Re because of your periodic claim visits. This makes you an important part of the marketing department. If you act professionally, competently and reliably, the cedant will tend to think of Total Re in the same way. Don't you make a judgment about your auto carrier based on how they handle your claim? It is the same way with reinsurers, believe it or not.

Pay the claim promptly if it is warranted. Total Re's business will grow only if it swiftly reimburses the cedant on valid claims. Most reinsurers generally require that the claim be paid within 5-7 business days after receipt of the claim. The cedant's senior staff can get very nervous if their reinsurer is slow to pay on legitimate claims or comes up with spurious reasons why it will not pay.

From time to time you will have a question on whether you should pay a claim. Express your reservations long before the request for payment comes in, if possible. A difference of opinion on a single claim should not interfere with overall good relations between your companies.

Provide added value. This is a part of marketing. For example, you probably have seen more large complex cases than the cedants' claim staff. Sharing your experience may prove useful to the cedant in handling a claim. But don't be a know it all. The cedant's claim staff usually knows a lot about their own business. Remember, also, that under the Follow the Fortunes clause in most reinsurance contracts, the cedant's claims handlers generally have the last word in how the case is handled. All you can do and should do is make suggestions. The cedant's claim staff can take it or leave it.

Total Re may have specialized departments to help its cedants with unique claims situations. These services will distinguish Total Re from the other reinsurers. Some examples of specialized claim services are a rehabilitation department, staff with considerable experience in large catastrophe property claims or a structured settlement department.

At Total Re, you will really be a part of the Marketing Department.

3. Actuarial. A lot of what you in do in claims is also what the actuarial group does: estimate the value of losses affecting your reinsurance contracts. The only difference is that you make estimates on claims one by one while the actuaries make estimates on claims — both reported and *unreported* — as a group.

As an honorary member of the actuarial department, you are interested in whether the cedant's individual case reserves are timely and adequate. Your advice to the actuaries on these issues will affect how they interpret the loss statistics. If you report that a cedant's claim staff is prompt and sensible in establishing and reporting their case reserves, the actuaries will feel more comfortable selecting the lower end of an estimate range. If the cedant is slow and unrealistic then the actuaries will opt for a higher estimate.

The actuarial department is also interested in whether there is a change in the company's reserving approach. Changes in reserve methods could include speeding up or slowing down the posting of full, mature reserves. Unless they know about these changes, the actuaries will interpret a sudden increase or decrease in the reserves as new and significant trend when it may be nothing of the kind. Only you can discover and report to the actuaries what the claim department is doing in setting its reserves.

At Total Re, you will really be a part of the Actuarial Department.

4. Accounting. You will be called upon to review and communicate payment and collection problems between Total Re and its cedants. That is an accounting function. You may think that such tasks are not within your job description, but you will become a valuable resource for both parties in avoiding misunderstandings and acrimonious disputes. On the one hand, the cedant will view you as a spokesperson for Total Re when querying the status of payment on outstanding claims. At the same time, Total Re may turn to you when they want a quick assessment of reinsurance accounting issues where a particular program's underwriting is tied to claims paid or reserves posted

At Total Re, you will really be a part of the Accounting Department.

5. Claims. If they insist on telling you that you are in the Claim Department, don't fight it. You will in fact be doing some things that are commonly thought of as "claims" functions. For example, you will review coverage issues, set reserves, make claim-handling recommendations, and conduct audits. But remember how these activities fit into the bigger picture at Total Re. What you do directly impacts the company's bottom line and don't forget it. It may sound trite, but you need to communicate and work together with underwriting, production, actuarial and accounting.

Finally, you asked for some advice on what to do and what to look for on claim reviews (some call them audits, but that sounds like the IRS to me.) Of course, you are reviewing the claims in your capacity as an underwriter, marketer, actuary and reinsurance accountant — not really as a claim executive. During a visit with a cedant, there are 3 distinct activities underway:

(a) Re-analyzing allocations and coverage under reinsurance contracts. There is sometimes wide latitude available to the cedant in judging whether a claim falls under a contract and how expenses are allocated. If this judgment is supportable and consistent with past coverage positions, then the reinsurer normally must go along with the decision. If it is not supportable, then an adjustment should be made in the amounts owed by the reinsurer. Reviewing the entire file gives a full picture of how these decisions were made.

(b) Establishing independent reserves on claims subject to the reinsurance contract. Establishing reserves on reported and unreported claims during the claim reviews is often more accurate because the entire file is available as is the staff handling the case on a day to day basis. If you disagree with the ceded reserve, you will set an Additional Case Reserve (ACR) on the claim to make sure Total Re is adequately reserved. Also, the cedant's claim staff can sometimes say in conversation what they would not write on paper so it is very important to discuss high exposure claims with the claim staff.

(c) Evaluating the quality of the ceding company's overall claims operation. All ceding companies are not created equal. To fully understand the quality of the cedant's claim operation, there is no substitute for an onsite visit to the ceding company's offices. Among other things you must review the timeliness and diligence of the cedant's investigation; the promptness and adequacy of the reserves; the cedant's attitude towards settlement (settle or go to trial); and, how quickly it reports claims to Total Re.

If possible, conduct your review at a desk in the middle of the claim department. That way you have immediate access to the person handling the claim. More importantly, you can pick up vibes by seeing how the claim staff interacts and works. If the reinsured company does not want you to be among them, be suspicious. You might ask what they are trying to hide. Of course, it may be that they just don't have any room for you and there is nothing at all to suspect."

You may deal largely with claim issues at Total Re, but you won't really be a part of its Claim Department.

Well that's it. Just remember you will be wearing many hats at Total Re including those of underwriting, marketing, actuarial and accounting and just a little bit of claims. Working in all of these departments simultaneously is a tall order (and you only get one pay-check) but I know you are up to the challenge.

Good luck. And don't be a stranger.

Jack