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Has the Insured Nailed It?

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IF PINTEREST HAS TAUGHT US ANY-thing, it is that failures can be funny. "Pinterest fail" is a common phrase, which references our flops — often in a self-deprecating, loving way. Netflix's show, *Nailed It!*, features every day, hapless home bakers attempting to recreate pastries which would make professionals walk out of the kitchen muttering under their breaths. Inspired by the 'nailed it' meme on Pinterest, the show highlights amateur bakers who can barely make edible cakes.

Unfortunately, when amateurs administer their insurance claims, the results could end up as 'failures'. There is no insured because there is no insurance policy for self-insured retentions (SIRs). The insurance client, generally a business with a well-developed risk management department, is the insured since liability claims are brought against it by a third-party claimant.

SIR AND DEDUCTIBLE DIFFERENCES

Many laypeople and insurance professionals are not familiar with SIRs. The insured does not have the same regulatory oversight as an insurer, and this aspect directly affects the principle of indemnity, good faith claims handling, and the superior knowledge of an insurance professional compared to a layperson.

SIRs are specific amounts insureds must pay before the insurer or overlying carrier will assume the handling of the file. In the 2010 California Circuit Court of Appeals, 4th District ruled SIRs are the "equivalent to primary insurance." In other words, policyholders are self-insured, and there is no insurance policy in effect until the retention amount has been exceeded. This distinction is important.

Since SIRs are primary insurance, many courts opine the insurers' duty to defend does not begin until the retention is exhausted, unlike policies with deductibles which state insurers have a duty to defend from "dollar one." In 2009, the Massachusetts Supreme Judicial Court confirmed in *Boston Gas Co. v. Century Indem. Co.* self-insureds assume the duty of providing their own defense until its retention is exhausted.

SIRs allow for reduced premium costs; increased policy limits; and self-awareness of risks since insureds pay losses out of pocket through the claims adjustment and the handling of defense dollars. The overlying carrier gives the insureds the 'Golden Chef's Hat' signifying it won the first round and that the overlying carrier trusts the insured to handle its losses.

REGULATORY OVERSIGHT

To be clear, insureds do not have an insurance policy when they self-insure.

Insureds do not need to be licensed to adjust their claims in some states. Therefore, there is no regulatory oversight of the insureds as they adjust claims and instruct counsel regarding the defense of lawsuits.

Even if insureds retained a third-party claim administrator (TPA) to handle the losses, that firm need not be licensed because it does "not adjust claims under a policy of insurance, as all monies used to pay claims are secured directly from the client." New York believes there is a difference because the adjuster is retained by the insured, not an insurer.

Nailed It! co-host, Nicole Byers, giggles when the contestants show their catastrophic results, but Jacques Torres, a noted French chef and judge, is excited because he can gently teach the baker correct methods to avoid future fails. Adjusters, by the fact they handle several thousand losses, have the same type of superior knowledge for claims. This knowledge is useless, unfortunately, if not utilized by insureds. As in New York, California does not consider self-insureds to be an insurer by its regulatory definition; so, insureds are allowed to ignore a loss, refuse to turn it in or instruct their adjusters to "delay, deny, defend" the claim. While this may horrify insurers, there is little they can do. All too often, the overlying policy does not have specific language dictating when self-insureds must notify insurers of claims that fall within the retention.

PANIC BUTTON

In the show, the worst baker from round 1 receives a panic button. When pressed, Torres will come and guide the contestant through the problem for three minutes. The adjusters having neither a policy, nor a license, nor regulatory oversight means there is not a panic button for guidance on claims handling. Adjusters no longer need to investigate the claim in good faith if the self-insured instructs them to send a declination letter for no other reason than the insured believes the claimants' losses are fraudulent. The adjusters are also free to use the insureds' interpretations of what should and should not be indemnified. This may be arbitrary and capricious.

This means there is no panic button for the overlying carrier. In some jurisdictions, self-insureds may not owe a good faith duty to their insurers to settle claims within their retained limits. As discussed earlier, insureds must exhaust the retention before the insurer's policy will step forward — indeed, before there is even coverage for the loss. Insureds know their liability is limited, and the insurer will pay for any judgment or settlement in excess of the retained amount. This is a tempting reason to delay, deny, or defend the loss because the insureds' exposure will not pass the retained limit.

Conversely, in *North American Van Lines, Inc. v. Lexington Insurance Company*, the Florida appellate court discussed the concept of bad faith and the obligatory duties of good faith handling, which it believed is inferred in insurance policies. The court made a point of stating "[t]he duty of good faith and fair dealing in an insurance policy 'is a two way (*sic*) street,' running from the insured to his or her insurer as well as vice versa." The court further stated its belief insureds were operating under an "insurance-type contract" because the contract was similar to indemnity insurance since insureds were obligated to undertake the defense of a suit. Finally, the court stated neither insureds nor overlying carriers could arbitrarily reject a reasonable settlement.

Contestants on the show often talk to themselves to calm their nerves. Self-insureds believe they know how to adjust losses involving their reputation and product. After all, adjusting claims is easy. Insurers willingly gave control to the insureds, and insureds can explicitly ignore the advice of claim administrators. Courts have admonished insurance professionals for their superior knowledge and failure to advise insureds of possible hazards. The insurance industry may be placing itself in hot water if it has superior knowledge and fails to inform insureds of coverage issues or of the hazards of handling a claim in a manner of bad faith. When a lawsuit with a punitive damages plea is filed, does the adjuster have an ethical obligation to inform the insured that, if the judgment is in excess of the retention, the overlying carrier will not pay that specific part of the loss? Most courts believe the insured cannot advise itself of coverage, and the adjuster is technically working for the insured. Is it a moot point if the insured would pay punitive damages regardless? Florida court grants carriers the ability to seek reimbursement from insureds if the claim should have settled within the retention. However, that requires another court case to determine when and if the claim could have settled earlier.

The adjusters handling the loss use insurance language to discuss the claim with the claimants. They will 'settle' and ask for a signed 'release.' The claimant will not know there is not an insurer who is (not) funding the claim; they, and most likely the trial attorney, will not understand this, which gives the insurance industry a bad reputation as the carriers are lumped in with the bad actors.

Insureds like SIRs for lower premiums; insurers are attracted to SIRs because it lessens claim volume. The insureds are defending what they feel is important, and the overlying carrier freely gives up the right to control a defense, settle the underlying claim, or even know of the lawsuit's existence until after the retained limit has been exceeded. Although there is no insurance policy for the retention layer, clear guidelines regarding communication for claim and lawsuit notification should be written into the overlying carrier's policy. Insureds must heed the guidance of the insurer and claim professionals to avoid a *Nailed It!* scenario and Pinterest fails.

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