

General BI Subjects

The Cost of Claims Preparation

Introduction

Business Interruption (BI) policies in New Zealand usually insure the cost of preparing both the BI and the property damage claims with a distinct policy item and a separate sum insured or sub-limit. Some are wider than others in their coverage. Because I have dealt with claims and the cost of preparing them from both sides of the negotiating table, I am pleased to comment on the benefits that are provided by the insurance of Claim Preparation Costs.

General Description

Insurance claims inevitably come at the “worst possible time”. Competing demands on limited management resources include damage limitation, business continuity, reconstruction or replacement of buildings, plant, and stock. And who then has time to deal with insurers and their loss adjusters, investigators, and consulting engineers, providing data and answers to each of them according to their often-conflicting priorities?

It is a stressful time of scarce resources and limited (usually) in-house expertise in the claims procedures. But the insurance implications of the damage cannot be deferred because it is also a “worst possible time” from a cash flow perspective as the business has to fund repairs and replacements of damaged assets and the ongoing expenses of the business.

Enter the loss adjuster!

Loss adjusters are appointed by the insurers to investigate and report on the circumstances of the claim, addressing matters, which might affect the insurers’ decision on policy response to the loss. Once the insurers have made that decision, the loss adjusters are instructed to determine the value of the claim, usually by monitoring the cost of reinstatement of damage but excluding any improvements and the costs of repairs to uninsured property. They also have a role in ensuring that the most cost-effective reinstatement options are used without limiting the insured’s policy entitlement.

In New Zealand the adjusters are usually very pro-active in driving the process instead of waiting to respond to a submitted claim. Their professional ability and obvious desire to assist the insured to achieve all it is entitled to under the policy usually generate a relationship of confidence and preclude the need for the insured to appoint its own experts to prepare and advocate its claim. However, if it chooses to do so or if it simply needs additional resource to prepare the claim, the costs are covered by an item such as:

“This Item insures costs and expenses reasonably incurred by the Insured for the preparation of claims under this policy and under the Material Damage policy(ies).”

Preparation or Negotiation

Some NZ policies add

“ including presentation, negotiation, certification and/or justification of claims made under the policy(ies).”

Other policies refer to “preparation”, alone, or specifically exclude “negotiation” of the claim. I can understand the exclusion. Perhaps the distinction envisages the classic division of responsibilities whereby the insured quantifies and submits its claim, which is then investigated, adjusted and negotiated by the loss adjuster. Even the words (adjusted and negotiated) are adversarial and what insurer wants to fund its policyholder to pursue a claim against it, for which the insurer believes that it has no liability or there is a difference of opinion on value?

At what point does claim preparation become claim negotiation?

Without the involvement of an independent claims consultant the preparation, presentation and negotiation between the insured and the loss adjuster are indistinguishable, occurring point by point through the process as each cost or issue is discussed and agreed. Negotiation only arises if positions have been reached and a difference of opinion remains to be resolved. Even when a claims preparer is involved, if an open and consultative process can be maintained, claim negotiation is only distinguishable from claims preparation after all information and analysis has been provided but “final” opinions or positions on the claim remain apart.

If an independent claims consultant prepares and submits the claim, from the point at which it is received by the insurer the process becomes “presentation”, followed at some vague point, by “negotiation”. The downside is that it can more easily become adversarial and negotiation from stated opinions on the rights and wrongs of the claim takes longer than achieving many small agreements as a continuum through the process.

The hope is that professional egos do not add to the delay.

I dealt with a claim recently in which an independent consultant was appointed to take “a watching brief” but not to prepare the claim. Insurers initially asked whether the consultant’s fees could be included in a claim preparation item that specifically excluded “negotiation”. However, they quickly agreed that a hard line on the distinction might result in his taking a greater role, actually preparing the claim, which would have pushed me into a watching and auditing role during which discussion of the calculation, argument over appropriate trends, etc, might all be considered part of claim preparation.

In conclusion, I don't think that the exact point at which quantification or preparation becomes negotiation can be defined with precision. The extremes are clear but there is a grey area in the middle.

Salaries and Wages

Many NZ¹ policies now include specific mention of the costs of the Insured's staff who are directly involved in claim preparation. This is not for the time of management in supervising or "project-managing" the repairing, rebuilding, and replacing of damaged assets and the resumption of normal business operations.

" Salaries, Wages and related Overheads of the Insured's employees are deemed to comprise costs of claims preparation."

I have heard the suggestion that Salaries, Wages and Overheads are insured under the Gross Profit Item and any reimbursement for claims preparation comprises the reimbursement of a normal cost. I agree! But I think this reference in a claims preparation item is so specific that the intention must be to pay for the insured's staff even when the cost is not additional to normal.

Payment of Salaries, Wages and Overheads of the insured's employees can possibly encourage the insured to use its own staff, gaining some fortuitous benefit from the claim (payment for an existing fixed cost) rather than introducing a consultant into the equation. After 30 years as a loss adjuster and only three as a claims preparer, I might be accused of bias if I comment further on the relative merits of outsourcing the claims preparation or retaining it in-house.

Sum Insured for Claims Preparation

This is definitely a frequently asked question. Unfortunately it is one to which my answers are unhelpfully vague. I can only suggest that the smallest policies should insure at least \$10,000 for claims preparation and the biggest should insure "a couple of million". A cost of \$200,000 or \$300,000 is not uncommon for claims in excess of \$10 million (combined property and BI) and although I have heard some horror stories about claim preparation costs I have not been fortunate enough to be the one who billed them.

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¹ I am careful to qualify my comments as relating to NZ BI policies because coverage for the cost of claims preparation in other countries is frequently more restrictive. It might be only reimburse the cost of providing data requested by the insurer or adjuster. I have also seen a specific exclusion of the fees payable to a "public adjuster".