

Cause and Effect

If the loss ratio is one of the leading measures of success in the p&c industry, why isn't your underwriting department talking to claims?

BY GLENN MCGILLIVRAY

In many insurance companies serving the Canadian market, the so-called 'silo' mentality is alive and well. (In fact, one may even find silos within silos as people often don't speak to or collaborate with those in their own departments, let alone those in other departments.) The underwriting department, for instance, often doesn't talk to the claims department — one of the more problematic manifestations of the silo effect, and one that can have several negative repercussions for a p&c carrier.

Wikipedia notes the definition of *silo effect* or *silo mentality* as “[A] phrase that is currently popular in the business and organizational communities to describe a lack of communication and common goals between departments in an organization. It is the opposite of systems thinking in an organization.”

According to Marcel Côté in *CA Magazine* (March 2002) “Generally, silos are an offshoot of decentralized management. Ambitious managers, responding to the objectives asked of



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them, pull those reporting to them along in their quest. As a result, their department's interest takes precedence over the well-being of the organization. Once one sector starts to see its own goals as more important than those of the organization as a whole, and when individualism predominates over team spirit, silos emerge.”

Côté stresses, “The results are not hard to predict. Lieutenants concentrate on their personal objectives and disregard those of the whole. Since they don't expect their peers to assist them in reaching their objectives, they in turn make little effort to cooperate with

other managers. Rather, they convey the message that achieving their department's goals is paramount and other departments can take care of themselves.” However, what Côté doesn't mention, and what will be concentrated on herein, are those silos that are created not just by managers with ulterior motives (i.e. those who wish to build and rule their own empires) but by those who unwittingly create silos because they simply do not know that interdepartmental synergies can reap rewards for them, their staffs, their departments and, ultimately, their entire companies.

Communication between claims and underwriting

Take the case of the oft-failed interface between underwriting and claims noted above. If underwriting (which, for the purposes of this piece, includes actuarial) doesn't converse regularly with claims, then underwriting doesn't learn anything from claims — a shame, because there is much to learn. (It's

important to note that the reverse can also be true, claims can learn from underwriting. But for the purposes of this article, we will leave that dynamic for another day.)

Consider contract wordings for one. As those insurers covering properties along the Gulf Coast learned after Hurricane Katrina (i.e. the wind vs. water question), ambiguous wordings can pose serious problems for insurance companies. Such wordings, which may have stood up decades ago in far simpler times or which had never really been put to the test, may not be clear enough in today's complex world where plaintiffs' attorneys regularly seek to capitalize on such weaknesses, and judges increasingly show disregard for the insurer's original intent. The end result could be that an insurance company may end up being forced by the courts to pay claims that the policy was never meant to cover. At the very least, the company may be forced to eat some heavy legal expenses, as it did with the now infamous *Citadel General Assurance Co. v. Vytlingam*, and *Lumbermens Mutual Casualty Co. v. Herbison cases*¹, which took several years and a lot of resources before finally being decided in the insurers' favour.

As wordings are being developed — especially for non-cookie-cutter, complex commercial and industrial risks — it would be imprudent not to solicit input from the claims department. It is claims that has to interpret wordings, and it is the department that would have to deal with the situation if the language is not clear or is out of date. Further, it makes no sense for the claims department to see a wording for the first time only after a claim is filed. Most senior claims experts have a great deal of experience and can add much value to the wording development process. The same holds for the development of new products.

Understanding experience

Another consideration is having underwriting learn from claims adjusters' individual experiences. It is important to note that in most cases it is the claims people that have their "boots on the ground" — i.e. they are the

ones out in the "real world" physically evaluating risks the company is looking at binding or for which the company must pay a claim. These in-person visits allow the claims professional to look at such things as location, use, construction quality, and local hazards to name but a few. Coupled with the claims professional's loss control expertise, such visits and knowledge can be invaluable to underwriters who, more often than not, are deskbound.

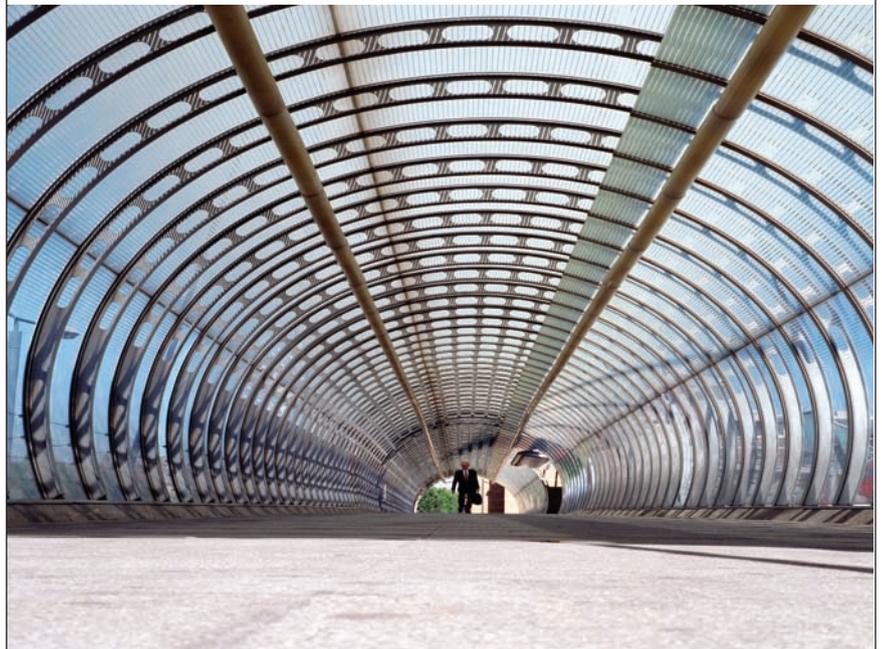
Similarly, claim audits/reviews (both

internal, conducted by, say, internal audit or finance, or external, conducted perhaps by the company's lead reinsurer) can be valuable sources of information, not just to members of the claims department under scrutiny, but also to the underwriting department. Such audits/reviews are intended to, first, satisfy senior management and/or a reinsurer that claims are being administered according to industry best practices and, second, to isolate any problem areas that need to be addressed. Under-



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writing can benefit from the process because it may help them get on or off a risk or category of risk more quickly, and to price risks more adequately. Also, such reviews can give underwriting a better feel for trends taking place in certain lines of business (like when there is a rash of claims occurring in a certain area). At the very least, underwriting should be copied in on the final audit report.

Keep underwriters in the loop

On a similar note, underwriting should also be copied in on any large-loss notices, and have a permanent seat at all claims department meetings. Insurance Claims Consultant Jim Cameron agrees. “There are still some insurance companies where the claims functions and underwriting functions are so far removed that we see an ‘us versus them’ attitude prevailing,” Cameron says. “This does not foster the cooperative approach which is vital to good commercial underwriting operations. Best practices include regular meetings between underwriting and claims and team approaches to the larger accounts from the outset.”

Also, it is usually part of the claims department’s job to monitor activity in the courts that have a bearing on the business of insurance. At the very least, it is common for claims professionals to personally take it upon themselves to watch such activity in order to spot trends that may impact how they do their jobs. Claims professionals often have an excellent sense of the structure of the legal system and legal trends in the jurisdictions in which they do business: How the justice system is set up, and how cases flow up the court hierarchy; Whether trials are by judge, jury or either and which is best; Whether a given court or particular judge in a given jurisdiction tends to favour the “victim”, particularly if the defendant is a “deep pocket,” regardless of fault, or whether the court is more balanced; How successful similar cases have been in the jurisdiction and the size of court awards in similar instances; Whether the court awards costs to the winning side; Whether class actions are the norm and, if so, whether they are easily certified etc. etc.

What’s more, the claims department often has a strong understanding as to when or under which circumstances arbitration is better than litigation and vice-versa. The claims department also often hears about court rulings sooner, and about those cases that are settled before formal proceedings began (and, often, what the details of the settlement were). As such, claims generally has an excellent sense as to, among other things, which types of risks, which lines of business or which geographic area should be avoided by underwriting, and how disputes between insurer and insured are best handled.

It is also common for a claims department to monitor emerging risks, most of which come on the liability side, but some of which may impact property covers as well. Claims experts often have a good sense of how the new risk is being handled in other markets

worldwide and can draw helpful parallels between the new risk and similar existing risks. Again, the claims department likely has an excellent sense as to which types of risks or which lines of business should be avoided by underwriting.

Additionally, as claims are filed after a significant loss event, such as a sizeable natural catastrophe, it often is the claims department that first identifies any problems regarding over-concentration of risk in a given geographic area. Over-concentration of risk, if not properly monitored and managed by underwriting, can be deadly to a company in the face of a large concentrated loss.

Conclusion

Though underwriting and claims departments each play very different roles in a p&c company (the former is there to bring money into the organization, while the latter is there to protect the company’s assets); it is crucial that underwriting has a clear understanding of what the claims department does and why it does it (particularly with regard to putting up and taking down reserves), and vice-versa.

And while it is true that the claims department has the benefit of 20/20 hindsight while underwriting doesn’t, one thing is certain: You don’t get claims without underwriting.

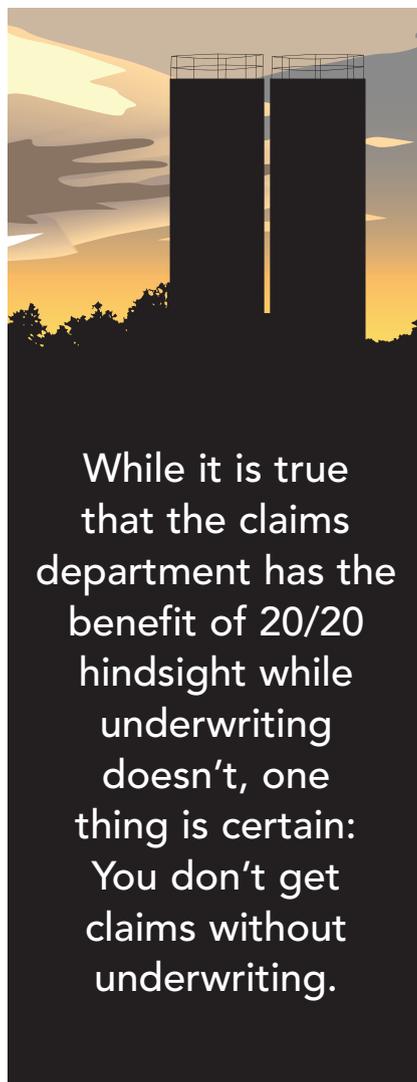
Still, claims professionals can work with underwriting to lessen the number (or, at least the size) of claims filed with the company.

Silos are best left for grain. 🍁

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Reference:

1. Canadian Underwriter Statistical Issue 2008, page 34



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