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FROM THE EDITOR

A Case for Experts

The property insurance claim has broken barriers in recent years, with far-reaching disasters that amount to enormous losses. There have also been tremendous changes to the way business gets done in a world more specialized and specific than ever before.

These trends suggest three things: That it is becoming increasingly necessary for insureds to obtain outside experts to help with claims. That qualified outside professionals can make a significant difference in the amount of a settlement and the speed with which it is reached. And that too many organizations fail to make sure their insurance program includes the coverage that will reimburse them for the costs of these services.

In this issue of Adjusting Today,® veteran loss consultant Harvey Goodman examines loss adjustment fees coverage by discussing how carriers take different approaches to this important protection. He also offers recommendations to the prudent insurance buyer who wants to make sure the coverage he or she is arranging will best respond to the needs of the business. The results of this analysis are detailed in this issue.

Sheila E. Salvatore
Editor



Proving an Insured Loss: Policyholders Need Experts Too Insure for this Additional – but Necessary – Expense

By Harvey Goodman, SPPA

Accidental damage to machinery at its Midwest plant leads to a complex business interruption loss for a metal processing firm. The firm initially struggles to calculate the damages on its own. Their claim is not accepted by the forensic accounting firm hired by the insurance carrier, whose settlement offer is only one-third of the insured's calculation.

To prove their claim, it is necessary for the insured to seek outside assistance at their own expense, as the cost to prepare and support their claim is not covered under their policy. The insured hires an engineer, a professional loss consultant and an accounting firm.



The claim is ultimately settled for an amount even greater than the insured's original estimate — and considerably more than the insurer's initial offer.

In two other instances, retailers — one on the West Coast and another in the South — suffered fire losses at major facilities. In settling their claims, both utilized the services of outside consultants to help determine inventory losses, establish the business interruption and extra expense claims, and adjust the loss — and both received favorable settlements. Yet their net recovery differed.

Because the West Coast firm had added a cost of loss adjustment expense endorsement to their policy, they were reimbursed for the costs of those services.

The retailer in the South, however, had to pay for the experts' services with their own funds, as was the case with the metal processing firm.

A devastating property loss can demoralize the management of any business. But compounding the problem all too frequently is the disappointment in discovering that the substantial expenses incurred in proving their damages to their insurer(s) are not normally covered by their property insurance policy. Historically, the costs of employing experts to prepare and support a claim are the insured's responsibility.

An Evolution

There was a time when property losses were settled quickly by experienced independent general adjusters who had sufficient authority to evaluate conditions using few, if any, outside experts. As the insurance industry evolved in the 1990s and 2000s, carriers began to use more and more outside specialists — including forensic accountants, engineers, contractors, testing laboratories, and so forth — to work with their own adjusters in evaluating a claim. Many factors contributed to this evolution, not the least of which was the carriers' desire to manage claim settlements using a centralized structure with claim-approval authority residing at the home office and not in the field.

To regain parity, insureds today find it increasingly important to employ their own outside consultants to help document and expedite their claims if they are to obtain a satisfactory claim recovery

and restore their business operations as quickly and completely as possible. Consequently, the use of experts — including accountants, engineers, industrial hygienists and public adjusters — has become a common procedure in property damage loss settlements. The fees of these outside experts, no matter how well-earned, can be an added burden when they are borne entirely by the insured.

Recognizing the Need

Fortunately, leading insurance companies have gradually come to recognize that their business policyholders do face increased financial exposure in preparing, supporting and settling a loss, and many carriers are now providing various ways to cover this exposure. Although some include varying degrees of coverage in the basic insurance form, more often than not, payment to the insured for loss preparation costs is regarded as not covered under the basic policy. Therefore, this important coverage must be addressed by adding an endorsement, which should be seriously considered when placing or renewing property insurance coverage. The insured may pay an additional premium yet closes a serious gap in their financial exposure following a property and/or business interruption loss.

The most common endorsement is the "Loss Adjustment Expense" endorsement, however similar coverage may be called "Professional Fees," "Claim Preparation Expense" and "Cost of Inventory and Appraisal." However, substantial variation exists among the many clauses and endorsements available, with some offering much broader coverage than others. It usually takes special diligence on the agent's or broker's part to make sure their client's policy provides the right protection. To that end, it is essential to understand what the variations are and how such differences can affect the insurance recovery.

Understanding the Intent of the Coverage

In examining the policies and forms of some 20 major property underwriters to see how coverage to reimburse policyholders for loss preparation costs is handled, it was interesting to see that some are quite detailed in their provisions, while others are remarkably brief.

What's more, the length of the endorsement does not necessarily reflect the true breadth of the coverage.

A good starting point for this insured is to construct a ‘what if’ scenario – projecting the maximum claim preparation expenses that might occur in the event of a loss.



And no matter how the extension of coverage is written, questions may still exist as to the exact intent and meaning of the language. To avoid potential conflicts, not to mention disappointment after a loss, before a loss occurs you can tell your broker your precise intent of the coverage. If possible, negotiate changes and clarifications to fit the insured's particular needs.

Focus on the Needs of the Risk Being Insured

As will be seen from the examples discussed in the next pages, a wide variety of clauses is available to cover the claim preparation costs needed to prove or support a property or business income loss. Some are included in the basic policy form or language; others must be added by endorsement.

In covering claim preparation expenses, think first about the specific exposures being protected against and the exact provisions that may be needed. Equally important, consider the limitations or exclusions that should be avoided. Knowing precisely what to anticipate is key to negotiating and securing the appropriate provisions.

Create Scenarios

The insured who has suffered a serious loss previously will have strong ideas as to the need for the coverage and the type of sources that should be insured for adequate protection — including dollar amounts of insurance. One who has never experienced a devastating loss, however, may face a far different challenge. A good starting point for this insured is to construct a “what if” scenario — projecting the maximum claim preparation expenses that might

occur in the event of a loss. Answer such important questions as:

- Are duplicate records available if in-house records are destroyed?
- Are inventory reports always available?
- Are these records reasonably up-to-date?
- Do staff have experience with handling complex claims — and do they have the time to handle a loss — or would outside expertise be required?
- What types of professionals are needed, i.e., accountants, appraisers, engineers, public adjusters, attorneys?
- Are these professionals readily available to the insured and how familiar would they be with their property and operations?
- What are the expected costs for employing outside experts?

Comparisons of Loss Adjusting Fees Coverages

To this end, we have collected and compared the loss adjustment fees coverage by discussing how carriers take different approaches to this important protection. We also offer recommendations to the prudent insurance buyer who wants to make sure the coverage he or she is arranging will best respond to the needs of the business.

Analyzed below are examples of several representative endorsements along with comments noting some advantages and disadvantages of each.

1. “Professional Fees. This Policy covers the actual costs incurred by the Insured, of reasonable fees paid to the Insured’s accountants,

architects, auditors, engineers, or other professionals and the cost of using the Insured's employees, for producing and certifying any details contained in the Insured's books or documents, or such other proofs, information or evidence required by the Company resulting from loss or damage payable under this Policy for which the Company has accepted liability, including consultant's services to the extent they are for producing and certifying any details contained in the Insured's books or documents, or such other proofs, information or evidence required by the Company resulting from loss or damage payable under this Policy for which the Company has accepted liability."

Comment:

Sometimes the insurer may dispute costs for items that were not specifically requested by the insurer. Also, sometimes there is language that excludes certain types of professional help.

2. "Professional Fees. This Policy covers the actual costs incurred by the Insured, of reasonable fees payable to the Insured's accountants, architects, auditors, engineers, or other professionals and the cost of using the Insured's employees, for producing and certifying any particulars or details contained in the Insured's books or documents, or such other proofs, information or evidence required by the Company resulting from insured loss payable under this Policy for which the Company has accepted liability."

Comment:

Similar to #1 but does not specifically mention "consultants." This provision clarifies that "auditors fees" are covered, subject to whatever limit is shown. It is not clear, however, whether the insurer intends "auditors" to be used in a descriptive sense — meaning anyone who "audits" or compiles figures, or in a more defining way, limiting the term to an actual professional "auditor."

3. "Claim Preparation Expense. Expenses incurred by the Insured or by the Insured's representatives including accountants, appraisers, architects, auditors, consultants, engineers or other such professionals in order to arrive at the loss payable under this policy in the event of a claim."

Comment:

Often the shorter the endorsement, the broader it ends up being.

4. "Loss Adjustment Expenses. This policy is extended to include expenses incurred by the Insured, or by the Insured's representatives, for preparing and certifying details of a claim resulting from a loss which would be payable under this policy."

Comment:

Check declarations for specific dollar limits on these coverages.

5. "\$_____ on reasonable fees payable for producing and certifying particulars or details of the insured's business required by the insurer in order to arrive at the loss payable under this policy in the event of a claim."

Comment:

This endorsement is obviously subject to a limit of insurance, which would be purchased at a level commensurate with the risk involved. There is no reference to a premium charge, and it is open-ended as to the types of services that are covered. Obviously, the term "reasonable" may prove troublesome in the execution of any claim.

6. "In consideration of an additional premium included, coverage under this policy is extended to cover any cost of inventory, appraisal, adjustment and preparation of loss data, not to exceed \$_____, in connection with any claim covered under this policy."

It is understood and agreed that the insurance granted under this endorsement is intended to cover any and all costs as mentioned above which the insured deems necessary in the event of a loss, and it is further understood and agreed that the insurance under this endorsement is not subject to the average (coinsurance) clause, if any, contained elsewhere in this policy."

Comment:

Like Example 1, this endorsement also limits the amount of coverage for fees, but it calls for an additional premium to be paid. Ostensibly, it places no limits on who may supply the services. The actual cost of the additional coverage as well as the limit of insurance are important factors to consider.

Several insurance companies use more complex endorsements to extend coverage for loss adjusting expenses. While the items in the form may vary to some

extent, the following example is representative of some of the more complex endorsements.

7. “Cost of Inventory, Appraisal and Adjustment

A. Coverage: In the event of a loss or claim to real or personal property, earnings and/or other property coverages included in this policy, this policy shall reimburse the insured for the following expenses incurred as the result of said loss or claim:

1. Any and all expenses incurred for the preparation of records or evidence to substantiate the amount of loss claimed. The insured shall be reimbursed for the expense of furnishing a complete inventory of destroyed, damaged or undamaged property, showing in detail, quantities, cost and providing the actual cash value.
2. In the event an appraisal is called for as set forth in the [standard policy, policy form, item X, etc.], this company shall reimburse the insured for the cost of the appraiser, the shared expenses of the appraiser, and the umpire.
3. Any expenses or fees, not to exceed 10 percent of the adjusted loss or claim, that are incurred by the insured as a result of the adjustment of the loss or claim. Coverage provided here in is not subject to any coinsurance or average clause which may be attached to this policy, but is subject to the limit of liability as set forth in [area where this information could be found in the policy would be stated].

B. Special Exclusions — Excluded or Uncovered Expenses:

1. Any and all expenses for taking inventory or preparation of any appraisal prior to any loss.
2. Attorney or legal fees, including court costs.”

Comment:

This endorsement provides broad coverage for loss adjustment expense, but limits the amount of insurance directly to 10 percent of the loss, however, not as an additional amount of insurance beyond the limit of liability. When a loss exceeds 91 percent of the policy limits, recovery of loss preparation costs, even if not exceeding 10 percent of the loss, could be reduced. If the loss equals or exceeds the limit of liability, no coverage is available for loss preparation costs. Note that any expenses relative to inventory or appraisals prior to the loss are not covered, nor are legal and court costs. Policies using this form may include a deductible that limits coverage.

Basic Considerations

Here are some questions to consider when researching loss adjustment expense coverage:

- | | |
|--|---|
| 1. Is this coverage provided by the basic property form? | and cover only outside professionals? |
| 2. Does the insurer offer coverage through an added endorsement? | 6. What kind of professional services are included: <ul style="list-style-type: none">• Lawyers?• Accountants or CPAs?• Architects?• Engineers?• Others? Does the endorsement cover the services of Public Adjusters? If so, for what services? (Know the specifics.) |
| 3. If coverage is by extension, is a separate premium charged? | |
| 4. Is there a limit of insurance applicable for this extension? If so, is it a fixed limit or variable? If it is variable, is it based on a percentage of the loss? And if so, what is the percentage? | 7. Is coverage for Public Adjuster services provided by the extension or by a separate endorsement? What is the approximate added cost, if any? |
| 5. Does the extension limit coverage to the use of the insured's own employees? Or conversely, does it exclude employees? | 8. Does the coverage limit assistance to only one area of coverage, i.e., business income, or does it apply to all insured property? |

Below is one of the more comprehensive endorsements reviewed from an excess policy developed by a surplus lines broker and it provided specific coverage for public adjuster's fees.

8. “Pays the named insured for any reasonable expenses incurred after a loss for the preparation of inventory of damaged and undamaged goods.” (The insurance policy requires this of the insured, but expenses are not always covered.)

“Reimburses the named insured for expenses incurred as a result of ‘going’ to appraisal.” (Under normal practices, the insured is expected to pay his own appraiser and 50 percent of the expenses of the umpire. These expenses are usually not recoverable under the insurance policy.)

"Pays up to 10 percent of the adjusted loss for the services of a public adjuster." (Normally the insured is expected to pay the public adjuster, but this coverage recognizes that the public adjuster performs many of the services the policy requires of the insured.)

Comment:

This form is very unusual with respect to its explanation of the coverage. It points out the inherent advantage of the coverage, which is extended specifically to cover public adjuster fees up to 10 percent of the amount of the loss, and to cover costs of any appraisal process which are not covered under conventional property insurance.¹

In contrast to the depth and clarity of the previous examples, the following "Loss Adjustment Expense" endorsement included in a policy issued through a national insurance broker may not serve business clients who require the services of a public adjuster very well.

9. "This policy is extended to include expenses incurred by the insured, or by the insured's representatives, for preparing and certifying details of a claim resulting from a loss which would be payable under this policy. However, this company shall not be liable under this clause for expenses incurred by the insured in utilizing the services of a public adjuster."

Comment:

While this clause has no limits, it is not clear whether these costs are subject to or apply in excess of the policy's limits. The intentional exclusion of coverage for public adjuster's fees prevents the insured from recovering a claim cost which may be required in a complex loss situation.

Some policies or packages include loss preparation costs in the basic coverage, usually under a clause referred to as, "professional fees." Following are some examples.

10. "Auditors Fees. We will pay reasonable fees you are obligated to pay your accountants or auditors, subject to the insurance stated below, for:

- A. Producing and certifying particulars or details of your business expenses, profits, or losses when
- B. required by us to determine the business loss you sustain; following
- C. a covered cause of loss of property at the premium stated below, causing such a business income loss, but

D. only when we have stated a limit of insurance in the declarations for business income insurance."

Comment:

This clause is intended for use with time element coverages. It limits coverage to the amounts which would be shown as limits of insurance for each location listed in the schedule, and to fees paid to "accountants or auditors." It is unclear whether the insured can be reimbursed for anyone performing accounting functions such as a public adjuster who prepares the business interruption claim.

11. "This policy covers the necessary and reasonable fees incurred by:

- A. The insured's customary auditors, accountants;
- B. architects or engineers with mutual agreement during loss settlement between the insured and this company's loss adjuster, except the insured's own employees, for producing, preparing and certifying details of a claim resulting from a loss payable under the time element endorsement coverage provided by the policy. This coverage is not subject to the reporting or adjusting clauses of this policy. Limits of liability for such professional fees shall not exceed \$_____ or _____ percent of the adjusted claim, whichever is smaller."

Comment:

This clause, also used with time element coverages, seems to limit payment to the four professionals cited, and specifically excludes the insured's own employees. Coverage is limited to the dollar amount listed or a percentage of the loss, whichever is smaller.

12. "Professional Fees Coverage. Amount of insurance under the Employee Dishonesty Coverage includes an amount payable to auditors/accountants, except the insured's employees, for producing and certifying particulars or details of the insured's business, as required by the insurer, in order to arrive at an amount payable in the event of a loss."

Comment:

This clause, which only applies to fidelity claims, is quite open-ended — with no limitation on the amount of coverage available or the type of outside professionals that are used. It specifically excludes the cost of using the insured's own employees.

13. “This policy is amended to include architects and engineers fees incurred in repairing a covered loss. Inventory and appraisal costs are included, in addition to public adjuster and consultant fees in any covered loss adjustment.”

Comment:

No limit is shown for these extensions other than any applicable policy limits. Public adjuster and consultant fees are also specifically covered.

Some of the selected policies and endorsements that we examined, while providing loss adjustment fee coverage, severely limit the amount of insurance. Examples 14 through 16 illustrate that point.

14. “We will pay the extra wages you pay your employees for preparing inventories and other loss data for completing our proof of loss. We do not cover any other expenses incurred in preparing or submitting claims.”

Comment:

*This clause is included in the basic property coverage form of one insurer. Entitled “Extra Expense, Expediting Expense and Loss Adjustment Expense,” coverage is limited to \$10,000 or 10 percent of the combined business real and personal property loss, whichever is less. Note that only expense involving employees’ work is intended to be covered, and not the cost of using outside auditors, public adjusters, or other professionals, unless the policy is specifically amended to that effect. However, in a case decided on appeal in New York State, *Tri Town Antlers Foundation v. Fireman’s Fund Ins. Co.* (7-10-90), the court, with two justices dissenting, found this language sufficiently ambiguous to allow recovery by the policyholder of \$8,709.14 of a public adjuster’s fees as “wages paid to employees.” Whether other courts would agree is a good question, so given the chance before a loss occurs, an insured, who would expect to use outside professionals in claim preparation, would do well to seek broader language that clearly includes coverage for the cost of outside professionals.*

15. “Cost of Preparing a Statement of Loss. You may extend the insurance provided by this coverage form to apply to the cost of a statement of loss or any other exhibits required under this policy. The most we pay for the cost of preparing a statement

of loss or any other exhibits is \$5,000 for any one claim. No deductible applies to this extension.”

Comment:

This clause is part of a basic property form, rather than an endorsement. It does not limit coverage to specific types of professionals. The \$5,000 limit is stated, in a later clause of the form, to be a separate amount of insurance, applying as excess over any other applicable coverages.

16. “Loss Data Preparation Costs. We will pay up to \$5,000 for reasonable costs you incur in preparing loss data required by policy conditions. This includes the cost of taking inventory, making appraisals and preparing other data to determine the extent of your ‘covered loss.’”

Comment:

This endorsement, with a fixed limit of \$5,000, is offered without charge to contractors, manufacturers/processors and wholesalers/distributors. The coverage applies to anyone providing the claim preparation service, including public adjusters and consultants. (Note that this insurer has taken the position that, while not stated in the endorsement, they will not pay fees for public adjusters calculated as a percentage of the loss.)

17. “Inventory or Appraisal. You may extend the insurance provided under this coverage form to apply to the following expenses you incur ... (1) the cost of taking inventories; (2) the cost of making appraisals; and (3) the cost of preparing a statement of loss and other supporting exhibits. The most we will pay under this extension for any claim is \$5,000. We will not pay for the expenses billed by and payable to independent insurance adjusters or for expenses to prepare claims not covered by this coverage part.”

Comment:

This clause, with a \$5,000 limit on coverage for loss data preparation, seems to exclude “independent” insurance adjusters. However, to avoid possible controversy, this should be clarified with the insurer.

18. “Cost of Preparing Proof of Loss. This form insures, subject to all its terms and provisions, for not more than \$10,000, any reasonable expense incurred in preparing proof of loss data or any other exhibits required in connection with any claim covered under this form.”

Comment:

This clause, with a \$10,000 limit on coverage, seems to include the services of any professionals used in proving and recovering a loss.

19. "Soft Costs Extension. Subject to the limit(s) of liability and deductible(s) shown elsewhere in this policy and to all other terms, conditions and exclusions not in conflict herewith, this policy is extended to cover soft costs which result from a delay in completions of a building or structure beyond the date it would have been completed had no loss occurred. This delay must be caused by a Covered Cause of Loss insured against by this policy to a covered building or structure in the course of construction or repair. Soft Costs mean only the following necessary and reasonable additional expenses: ... C) additional architect, engineering and consultant fees which become necessary as a result of an insured loss. ..."

Comment:

This clause is taken from a policy issued by United Insurance Consultants, Inc. Coverage for consulting fees includes part of an extension for "soft costs."

A Recommendation

Once the potential for the loss adjustment expense exposure is evaluated, it is wise to explore the options offered by a number of carriers. In the absence of a more acceptable endorsement, the insured should suggest the addition of this simple yet comprehensive wording to their policy:

Cost of Recovery — SES Insurance (your insurance carrier) will pay your reasonable expenses to recover a claim covered by this policy. This payment is limited to 10 percent of the amount of the insured claim. Legal fees for litigation and court costs are not included by this endorsement.

¹ In some states such as Virginia, if an insurance carrier requests an "appraisal" under the terms of the policy, the state statute requires the carrier to pay for both appraisers as well as the umpire.

Summary

More and more, insurance companies are using experts to support their side of a claim settlement, so it behooves today's policyholder to take advantage of similar professional resources to help prepare, support and settle their claims. Understanding and utilizing the coverages available for this purpose can help protect the insured not only against financial loss, but for the cost of recovering it.



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