



Claim Reserving

“Is that the amount we are going to pay the claimant?!”

Claim reserving is an art form coupled with an educated guess of the most probable outcome for any given claim. Reserves are set by insurance adjusters. For larger and more complex claims, a claims manager or vice president will approve the final reserve. Initial reserves are generally set within the first 30 days of a notice of claim. They are updated periodically based on new information, broker claim reviews, or depositions during litigation.

Workers’ compensation claims are a function of administrative law. General liability claims are in the civil arena where comparative negligence and general damages can dictate the value of a claim.

General Liability Claims

General liability claims have two primary components: Liability (comparative negligence) and Damages (economic and noneconomic).

Liability for claims is usually evaluated based on current laws (state statutes and case law) along with the comparative negligence conclusions from an insurer’s investigation. An insurer’s initial investigation can include recorded statements, official reports, photographs, diagrams, expert opinions, and other relevant information. The outcome of this investigation is usually challenged by opposing lawyers, and the final determination regarding fault is sometimes decided by a trier of fact (a trier of fact is a judge or a jury).

Damages are separated into two components; General damages (subjective) and Special damages (objective): General damages are noneconomic damages and can be classified as pain and suffering, loss of companionship, disfigurement or mental impairment. Special damages are economic damages (an objective number) that are specific expenses incurred or to be incurred by the claimant or plaintiff, such as medical bills and present and future wage loss. These expenses are supported by medical and diagnostic reports, hospital records, and income documentation. Special damages (economic damages) are much easier to project than general damages (noneconomic damages) since they are usually fixed and quantifiable.

General Liability Claim Example: A 30 year old female plaintiff sustains \$45,000 in medical expenses, and \$5,000 in past wage loss, for special damages of \$50,000. The plaintiff sustained a sprained wrist, one closed reduction for a broken lower right leg, and one closed reduction for a broken right ankle. She has made a full medical recovery. The general damages (for her pain and suffering) could range from \$75,000 to \$150,000. Maximum exposure would then be \$200,000 (the combination of economic and noneconomic damages). Your insurance company may conclude that your company is at least 50% at fault for her accident. Accordingly, your insurer might reserve the claim file for \$100,000 (50% of the maximum exposure of \$200,000).

Workers' Compensation Claims

Since workers' compensation is a no fault administrative system, the employer's insurer (the insurer stands in the shoes of the employer) is liable for a claim if it occurred during the course of employment, and arose out of the employment of the injured worker.

For workers' compensation claims, the medical costs incurred are special damages (economic damages), and special damages also include temporary total disability benefits (time off work). The permanent disability (PD) rating of the injured worker is measured by a percentage. PD benefits are set by law. PD benefit amounts in California, as an example, are determined as follows:

- The date of the industrial injury is a measure of what is allowed to the injured worker.
- The medical opinion from an injured worker's primary treating physician or a doctor who is a qualified medical evaluator are the key players to establish a rating. In other words, the doctor that has examined the injured worker and has determined his work impairment level then expresses a permanent disability rating in the form of a percentage.
- The percentage is used in a formula which also includes the age and occupation of the injured worker. For injuries on or after April 19, 2004, and prior to January 1, 2013, the formula also includes diminished future earning capacity.
- For dates of injury on or after January 1, 2013, PD ratings will no longer take into account an injured worker's future earnings capacity. In addition, injured workers are no longer able to collect additional PD for sleep disorders or sexual dysfunction that did not result directly from injuries. Additional PD for psychiatric injuries is limited to cases in which the physical injury is catastrophic or where the injured worker was the victim of or a witness to a violent crime.

A disability evaluator or an administrative law judge will calculate this formula and determine how much PD the injured worker is entitled to receive for the claim.

The medical costs, temporary total disability, and permanent disability are all special damages. Accordingly, the adjuster is responsible to evaluate the medical treatment, time off from work (temporary total disability), plus consider the overall extent of the bodily injury (permanent disability) to determine a reasonable reserve.

If your employee's injury was caused by a third party, your workers' compensation insurer may be entitled to subrogation (recovery rights) from a third party after the injured worker has become medically permanent and stationary, and the workers' compensation claim is settled. Keep in mind, that the reserve is not reduced by a potential subrogation recovery. Instead, you will see the benefit of the recovery as a monetary credit against the loss after the claim has been paid by your insurer. The same method of recovery is used for general liability claims.

Multiple Factors can influence claim reserves:

There are a lot of moving parts. Some adjusters are better than others when performing their evaluations. New facts can dramatically change the playing field. Potential motions for summary judgment can become interesting legal issues; meaning a civil court can grant a dismissal of a lawsuit pending against your company. The jurisdiction for any given claim is also another big factor. Just about anything can happen. Nonetheless, a reserve is still required based on the best possible information available to the adjuster.

Does the reserve mean that amount will be paid to a claimant?

Maybe. Settlements are typical, but sometimes there will be little or no payment by your insurer. Why? The reserves reflect probable outcomes that are not absolute. On occasion your insurer may experience defense verdicts that were unexpected. Another positive outcome would be a settlement that was very favorable to your company. Both will reduce your loss experience since the claimant was paid less than the reserve.

Keeping Reserves Low:

The first step in keeping reserves low is performing a complete accident investigation including witness statements and photographs. This helps to determine if any other party is responsible for the injury or accident. We provide our clients with ICE (In Case of Emergency) cards to facilitate prompt contact with PentaRisk and insurers to trigger a thorough investigation of a claim.

From there, our intrinsic value comes from knowing jurisdictions and potential outcomes. We have the depth of knowledge to understand your exposure for workers' compensation and general liability claims. We use this advantage to influence insurance adjusters regarding reserves. With our working knowledge of the claim process, we can help you achieve the best results to contain your loss experience.

Contact your PentaRisk broker or account executive for more information on *Claim Reserving*. Visit our website at <http://pentarisk.com/>.

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